



THE IMPACT OF CORPORATE GOVERNANCE MECHANISMS ON DEBT'S COST: EVIDENCE FROM CHINESE STOCK MARKETS

Waleed N. Mohammed

College of Business Administration and Economics
University of Samarra
waleed@uosamarra.edu.iq

Article history:		Abstract:
Received: 28 th November 2025		This research examines the impact of corporate governance mechanisms on the cost of debt of listed companies in Shanghai and Shenzhen stock exchanges. Indicators assessing the quality of corporate governance as well as related qualities are used to indicate their mechanisms. Effective corporate governance, as per the principal-agent's theory, can reduce information asymmetry and concern of shareholders. A sample of 10,630 Chinese firms for the year reference of 2021 to 2025. Further the STATA 13 was used to analyze the data. The analytical study further consists of all kinds of statistical descriptions and correlation information. It also includes an OLS Regression analysis. The key finding notes a strong negative association between corporate governance mechanisms and cost of debt suggesting that firms with able corporate leaders incur a lower cost of debt. As such, the study recommends for corporations to expand boards in other to reduce costs and enhance financial efficiency.
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Keywords: Corporate Governance, Corporate Governance Quality, Debt Cost and Chinese Firms

INTRODUCTION

Corporate governance is a very important subject of research area because of impact of corporation on this subject. Research has assessed numerous things such as the shareholders, supervisory board, management compensation, corporate governance, social media and so on (Bebchuk & Weisbach, 2010; Paniagua et al., 2017). This research's theoretical framework and hypotheses are derived from principal-agent theory, a very popular theory of leadership stud.

According to this theory, companies with multiple owners suffer due to lack of control over usage of their resources. Although they help to solve the problem of corporate governance, supervisory boards create other problems, such as information asymmetry. This refers to the classical problem of principal and agent who are different from both the owners and managers. The findings suggest that financial performance is influenced significantly by the corporate governance and financial reporting.

Per C. According to Chen (2010), firms listed on the Chinese stock exchange have their internal corporate governance structures more similar to the Anglo-American model. Y. L. A study of corporate governance in China in comparison with other OECD countries is conducted by Zhang, Ouyang and Tan (2009). In the process of the study, they found that many of the big companies in China have changed governance. Consequently, it is vital to comprehend the impact of corporate management on the cost of capital. Debt, preferred stock, common stock, equity and many others are types of capital expenditure. The paper looks into the relationship between firms' leadership and their debt costs recognizing the importance of debt costs.

The significant of the study

Nowadays, there is a rapidly interest about the corporate governance and how it is reducing the risk and improve the performance. So, that will reduce the credit risks that what the creditors considering in their perspective. Therefore, this study has significant from focusing on the Chinese firms in Shanghai and Shenzhen stock markets which is has special case due to the economics. It is also has new combined of corporate governance index.

The study problem

This research tries to answer the questionia: although the corporate governance (GG) issue is pressing, it is still unclear how GG mechanisms affect the cost of debt of firms with complex institutional arrangements, such as Chinese firms. There's an ongoing research on how GG influences borrowers' decisions.



This study's overarching research query is: How do mechanisms such as the GG impact the debt cost of Chinese firms? It furthermore casts doubt on the following: (i) What is the effect of corporate governance on the cost of debt? (ii) How does the corporate governance index influence the cost of debt?

The research objectives

There are several objectives of this research such as:

1. Checking the Corporate Governance Mechanism of Chinese Corporations
2. Exploring the impact of sound corporate governance on debt and financials
3. Investigating the Principal-agent theory relationship between Corporate Governance Index and costs of debt.
4. There is evidence showing that the quality of political decision-makers and investors is improving.

Hypothesis development

What is the link between corporate quality and debt costs? According to past studies, firms with good internal governance are found to have lower equity costs, so they are also found to have lower debt costs. This indicates that companies with a higher standard of corporate governance are less leveraged than companies with lower standards of corporate governance. This means that the additional benefit of preferential loans will be less favourable for companies with better corporate governance as compared to those with worse corporate governance. We propose that corporate leadership reduces debt costs, which this investigation finds is not true. The following hypothesized models are proposal.

Hypothesis 1: The expense of debt is affected significantly by the quality of corporate oversight mechanisms.

Hypothesis 2: The debt cost is significantly affected by corporate governance index of the firm.

Research Model

According to hypotheses in the section above, the research use the regression models are:

$$CsD = \alpha_0 + \alpha_1CGI + \alpha_2SIZE + \alpha_3LEVERAGE + \alpha_4CEODUALITY + \alpha_5years\ dummies + \epsilon \quad (1)$$

$$CsD = \alpha_0 + \alpha_1CGQ + \alpha_2SIZE + \alpha_3LEVERAGE + \alpha_4CEODUALITY + \alpha_5years\ dummy + \epsilon \quad (2)$$

The table (1) demonstrates the meanings of variables

Table (1): Variables Definitions

Variables	Definition
DsC	finance expense/ average short-term + long-term debt
CGI	Governance index measurements from 1 to 17
CGQ	1 if the corporate's income is higher than the average of CGI, and otherwise 0
SIZE	The natural log of the total assets.
LEVERAGE	The total sum of short and long term debt is divided by the total assets.
CEODUALITY	If the CEO is also the chairman of the board, the number is 0.

Research Model is showed in the figure bellow:

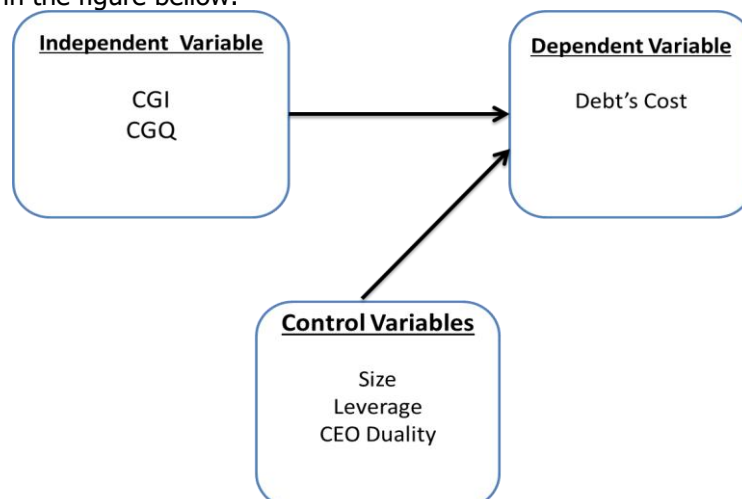




Figure (1); Research Model (source; created by the author)

Sample

The sample contains all Chinese listed companies listed in the Shanghai stock exchange and Shenzhen stock exchange and the complete Chinese population. The CSMAR database was used to collect data from 2021 to 2025 in relation to the other listed companies. Financial institutions were prohibited as the regulatory scheme to which other businesses were subject was dissimilar. Institutions without data were also excluded from the analysis. A total of 10,630 firms make up the final sample..

VARIABLES MEASUREMENT

Debt’s Cost

According to past studies, debt cost has been determined by dividing the interest cost by the average short term and long term debt for a current financial year (Liedong & Rajwani, 2018; Al-Delawi, 2023). The short- and long-term debts are obtained from the company’s financial statements in the CSMAR database while the interest expenses are obtained from their income and loss.

Quality of Corporate Governance

According to the guidelines of the Howard Report, the CGI (Corporate Governance Index) is calculated. CGI evaluates the quality of corporate governance of the surveyed companies. The index primarily focuses on whether the organization has improved the quality of internal processes and systems. According to the Howard report, the analysis was conducted under six heads or categories. The supervisory board structure, audit committee composition, nominating committee, compensation committee, independence of the external auditor, and code of conduct and other requirements for disclosures is proposed in R62 to R68 for the SEBI LODR regulations. The 17 criterion for governance are found in the Howard Report categories. To generate the CGI we employed a scoring or rating method which attributes the same weighting to each qualitative observation, also used in the existing corporate governance literature (Gompers et al., 2003) If a corporation’s goal is achieved, it scores 1, otherwise 0. As an illustration, if the majority of directors are self-governing, the corporation is deemed to possess a value of one, otherwise the value is zero. All the numbers are summed up to form a corporate governance index that ranges from 0 to 17. Here, 0 means poor quality of corporate governance whereas 17 means high quality of corporate governance. Each of the measures’ figures make up the overall score for each of the board, audit, nomination, compensation quality of governance..

Control Variable

As per the literature on the costs of debt (Pittman & Fortin, 2004, Qiu & Yu, 2009), a regression model which considers various variables as controls seems appropriate. Namely: total balance sheet (size of the company), debt ratio (leverage), and duality of the general manager (CEO duality)..

ANALYSIS RESULTS

Descriptive Statistics

Table 1 presents the descriptive statistics of all Chinese firms which were included in the study. Average CGI and QCG values are 13.135 and 0.805, respectively..

Table (2): Descriptive statistics for the entire list of companies

Variable	Obs	Mean	Std.Dev.	Min	Max
CGI	10630	13.135	5.554	0	17
QCG	10630	.805	.396	0	1
CoD	10630	7.06	6.967	0	22.024
Laver.	10630	.206	.153	0	3.064
Size	10630	22.242	1.318	16.52	28.036
duality	10630	1.784	.412	1	2

Correlation

Table 3 shows the extent to which there is relationship between the various variables in the sample. The figures in the table registering corporate governance variables are negatively correlated with the cost of debt. Another important determinant of quality of corporate oversight is the debt to equity ratio. Corporate Governance Quality (CGI) and Corporate Governance Quality (QCG) are negatively associated with company size and revenue, and positively associated with both.

Table (3): Pairwise correlations

Variables	(1)	(2)	(3)	(4)	(5)
(1) CGI	1.000				



(2) QCG	0.941	1.000				
(3) DsC	-0.082	-	0.073	1.000		
(4) Leverage.	-0.016	-	0.037	1.000		
(5) Size	0.088	0.085	0.184	0.135	1.000	
(6) CEODUALITY	0.005	0.061	0.168	0.039	0.165	1.000

Regression Results

Table 4 shows the results of a multivariate regression analysis that uses the complete list of companies in China to measure the costs of debt financing in relation to the quality of corporate governance (CGI and QCG). This table has two columns because QCG and CGI are two separate components of each other. According to the findings, there is an inversely proportional association between the quality of corporate leadership and the cost of debt payments. Models 1 and 2 use the multiple regression result to investigate the relationship between the expense of debt financing and corporate governance quality to test the hypothesis. The coefficients of both corporate governance indices (CGI and QCG) are negative and statistically significant (- 0.129, t = -10.39, p < 0.01 and -0.152, t = -11.36, p < 0.01 respectively) supporting the sixth hypothesis. According to Chen et al. (2009), firms with a good level of private control over government suffer less overall risk from government assistance – this reduces borrowing costs. From a corporate governance point of view, these findings are consistent with this.

Table (4): OLS Regression Analysis Results

VARIABLES	(1) CoD	(2) CoD
CGI	-0.129*** (-10.39)	-0.152*** (-11.36)
QCG		
Leverage.	-0.964** (-2.119)	-0.983** (-2.161)
Size	0.855*** (16.41)	0.877*** (16.68)
duality	2.422*** (15.02)	2.462*** (15.21)
Year Dummy	Yes	Yes
Constant	-13.36*** (-11.48)	-13.46*** (-11.45)
Observations	10,631	10,631
R-squared	0.072	0.075
r2_a	0.0711	0.0740

t-statistics in parentheses

*** p<0.01, ** p<0.05, * p<0.1

RESULTS DISCUSSION



The results of this study shows there is a negative and significant relationship between the corporate governance mechanisms and debt cost even for quality and index of corporate governance. From the debtors perspective, the firm with high quality of corporate governance has low risk leading to obtain the low cost of debt (Ashbaugh-Skaife et al., 2022; Huang & Zhu, 2024).

These results consist with the agency theory that assumed improving the control and transparency tools will reduce problems between the management and shareholders (Chen et al., 2023; Liedong & Rajwani, 2022). The previous studies found that the good governance will reduce the systematic and unsystematic risks thus, this research results consist with their results because when a firm has low risk that lead to low cost of debt (He et al., 2023; Shan & Walter, 2023).

CONCLUSION

In summary, it can be concluded as below:

- 1- The research found that the high quality of corporate governance leading to reduce the cost of debt these results consist with literature about good governance mechanisms reduce the agency risk and information asymmetric.
- 2- The results shows that the corporate governance index is good tool for explain the why there is a difference between the cost of debt in firms
- 3- he results also indicate the CEO duality outcome has a high cost of borrowing due to control diminishes.

RECOMMENDATIONS

The research suggest some recommendations as below:

- 1- It is necessary to enhance the quality of corporate governance especially, the board independency and activate its committees
- 2- It is necessary to use the composite governance index when the firms evaluate the financial performance and credit risks.
- 3- Separating the position of CEO and Chairman of the supervisory board is important, as it will improve internal control and reduce the cost of debt..

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