

Analysis of the Impact of Good Corporate Governance and Bank Fundamentals to the Financial Performance of Banking Institutions in the Indonesian Stock Exchange (BEI)

Wawan Purwanto
Program Studi Magister Manajemen, Fakultas Ekonomi dan Bisnis, Universitas Mercu Buana Jakarta
E-mail: wwnpwt@gmail.com

Abstract
This paper analys the impact of good corporate governance and bank fundamentals to the financial performance of banks. The airm of this research is to give empirical proof and Determine whether good corporate governance represented by some of independent board of commissioner, the audit committee and risk monitoring committee and bank fundamentals can be indicated by the increase of in total assets, loan to deposit ratio (LDR) and return on equity of previous year also Significantly Affect to financial performance of banks.This study uses statistical and mathematical analysis with financial performance represented by the ROE as the dependent variable and independent board members, audit committee, risk monitoring committee, increase of in total assets as well as loan-to-deposit ratio and return on equity of previous year as an independent variable. This research usen 19 banks listed on the Indonesia Stock Exchange from year 2007 to year 2012.The result of this study shows that good corporate governance and bank fundamentals simultaneously significantly affect bank performace. Increase in total assets and return on equity of previous year significantly affect to individually bank performance.
Keywords: GCG, Bank Fundamentals, Financial Performance of Banks.

Introduction

Disclosure of corporate information openly is important for public companies as a form of transparency and accountability of management company to stakeholders. Stakeholders are all of parties interested to the survival of the company. Full disclosure of corporate information is very useful to stakeholder for consideration in decision-making (Almilia and Retrinasari 2007 in Lestari 2011). Good corporate governance is a concept which emphasizes the importance of the right of shareholders to obtain information that is true, accurate, and timely. It also shows the company's obligation to disclose all of the company's financial performance information accurately, timely, and transparent. Therefore, both public and closed company do should look that good corporate governance (GCG) not merely as an accessory, but it should be seen as an attempt to improve the performance and value of the company (Tjager, 2003 in Lestari 2011).

Corporate governance is one of the key elements in improving the economic efficiency , which includes a series of relationships between corporate management, board of directors, shareholders and other stakeholders. Corporate governance also provides the structure that facilitates the determination of the company objectives and performance monitoring techniques (Darmawati et al., 2004, in Lestari 2011). Forum for Corporate Governance in Indonesia (fcgi, 2001) formulate the purpose of corporate governance is to create added value for all interested parties (stakeholders). Corporate governance contains four important elements of justice (fairness), transparency (Transparency), liability (responsibility) and accountability (accountability), which is expected to be one of the ways to minimize the agency conflict (Andriani, 2007).Generally, the company's survival is strongly influenced by corporate governance. In many cases, the collapse of the business and corporate scandals anywhere in the world proven to have anything to do with good corporate governance (GCG), where GCG principles are universally that are not implemented purely and consistent (Sugiarsono 2009 in Lestari 2011).

Good corporate governance (GCG) is very important to be applied in a company, because each individual, basically, tend to be selfish. This as the cause of a conflict of interest between the principal (shareholders or investors) and the agent (management of the company). Principals have an interest to maximize their profits while the agency has an interest to maximize their economic and psychological need. Furthermore, The conflict will continue to increase due to the principal does not have the ability to oversee the daily activities of an agen and ensure that the agency has been working in accordance with the wishes of the principal. One way to reduce the conflict between the agent and the principal is through disclosure by management (agent), which is in line with the development of corporate governance issues. It is expected that the agent can work to meet the demand of the principal. This will increase attention to the issue of disclosure on corporate governance aspects of a company.

Stock exchange is an institution that uses the system with an operating complex but still maintaining governance (corporate good governance) which is good for the public company. Good governance includes; serving that minority shareholders receive reliable information about the rvalue of the company. They have confidence that majority shareholders are not deceptive and will not make them forced to withdraw their investment from companies. And motivating managers in order to maximize the value of the company is not just looking at the target profit earned

Transparent financial accounting information is the product of the company's financial accounting and external reporting systems are measured routinely. This report is audited, as quantitative data that describe the financial position and performance of the company that owned such banking sector. The results of the analysis of how the audited balance, income statement, and statement of cash flows, together with the supporting disclosure. Financial performance report information used as a basis for information-company regarding certain aspects of performance that are useful to investors and regulators. Develop and maintain financial performance in a specific assessment system in a systematic and sophisticated is not cheap. Countries with highly developed securities market devote resources are expensive to produce and regulate the use of the rules of financial performance that can be followed by a large public company. Resources are used not only financial, but also include opportunity costs associated with the deployment of human resources who are well educated, including accountants, lawyers, academics, and politicians.

Literature review

Agency theory is used to understand the basis of corporate governance. Agency theory regarding the contractual relationship between the members of the company. Jensen and Meckling (1976) in Adriani (2011) explains that the agency relationship arises when one or more persons (the principal) employs another person (the agent) to provide a service and then delegate decision-making authority to the agent. While Hendriksen and Michael (2000) in Adriani (2011) stated that the closing agent contract to perform certain tasks for the principal and the principal closing contracts to reward agents. The so-called principal shareholders or investors, while the agent in question is the managing company management. The essence of the agency relationship is the separation of functions between ownership on the part of investors with management control.

The audit committee of a company is responsible for the company's financial reporting. With the audit committee of management will minimize the possibility of earning management by way of supervision over financial reporting and oversight of the external audit.In accordance with Kep. 29 / PM / 2004, the audit committee is a committee established by the board of directors to carry out the task of monitoring the management of the company. In addition, the audit committee is considered as a liaison between the shareholders and board of directors with management in order to overcome the problem of the possibility of control or agency. Based on the circular JSE, SE-008 / BEJ / 12-2001, the membership of the audit committee consists of at least three people, including the chairman of the audit committee. The committee members are derived from the commissioner just as much as a person, committee members from the commissioner is independent of listed companies as well as a chairman of the audit committee. Another member who is not an independent commissioner should come from an independent external party.

Sitinjak (2007) states that the independent variable (Score GCG) and control variables (size of assets, the opportunity to grow, and the size of the company) a significant effect only on Revenue Growth. Thus, it can be concluded that corporate governance affects the operational performance of the company.

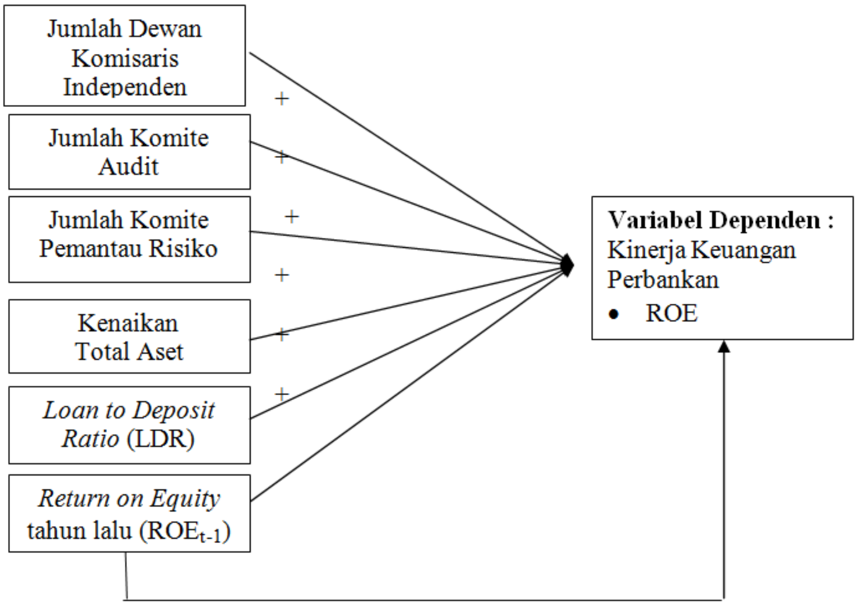
A study by Anup Agrawal and Charles Knoeber, who tried to statistically control for the endogeneity problem of corporate governance, further results are contrary to the trust management. they find that there is a negative impact on financial performance when the system of governance council positions too many directors who come from outside.

In managing good governance in the company needed four aspects of sustainability assessment that must be passed and analyzed, namely: social influence, which is defined as a measure of the impact that people interact with Integration in terms of the social contract and the influence of stakeholders;environmental impact, which plays an i the impact of corporate actions on geographical environment. Organizational culture, can be defined as the relationship between the company and internal stakeholders, particularly employees, and all aspects of the relations; Financial aspects, defined in terms of a reasonable return to the level of risk undertaken.

Other opinion is when the institutional arrangements favor mandatory versus voluntary corporate disclosure, this study suggests a reform measure for the East Asian corporate governance system that relies, inter alia, on the percentages of long‐term and short‐term financing to total financing. The higher the percentage of long‐term financing, the more we can infer the extent of outside investors' confidence in the future of the East Asian firms. When more active role of banks involvements with the firms' business is permitted and an effective banks' and firms' strategic transparency can be assured, the East Asian banks and stock market can both lead firms to long‐term favorable achievements. This study also suggests that the protection of both shareholder's rights and creditors' rights can go in parallel lines with the latter is to be given first priority until the investors' confidence in the near and far future of East Asia corporate governance system is built.

Theoretical Framework
With a view of the basic theory outlined earlier and previous studies, indicate that there are various factors that affect financial performance. This study examines the factors that affect the financial performance of banks listed on the Indonesia Stock Exchange (IDX) as measured by the independent board, audit committee, risk monitoring committee, the increase in total assets, loan to deposit ratio (LDR), and Return on Equity last year. So that the framework can be described as in Figure-1.

Figure-1
IndependentVariables:Corporate Governance and fundamental indicators of banks



Source: Developed for this research

Hypothesis
1) The number of independent board positive effect on the bank's financial performance measured by ROE.
2) The number of audit committee has positive influence on the bank's financial performance measured by ROE.
3) Total risk monitoring committee has positive influence on the bank's financial performance measured by ROE.
4) The increase in total assets has positive influence on the bank's financial performance measured by ROE.
5) Loan to Deposit Ratio (LDR) positive effect on the bank's financial performance measured by ROE.
6) Return on Equity last year (ROEt-1) positive effect on the bank's financial performance measured by ROE.

Methodology
Research conducted in the field by collecting data obtained from annual reports published during the banking 2007-2012 period. Data collection was conducted in May 2013.

The variables used in this study is two independent variables (X) and the dependent variable (Y). The independent variable was the fundamentals of good corporate governance and the bank while the dependent variable is the financial performance of banks. After the determination of the variable is then determined scale of measurement. In this study, a scale of measurement that will be used is the ratio scale.

In this study banking financial performance is measured by using ROE (Return On Equity), where a high ROE describe the performance of good banking. ROE is calculated using the following formula:

$$ROE = \frac{NetIncome}{TotalEquit\ y} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(2)$$

The population of this study are all companies listed on the Indonesia Stock Exchange during the period 2007-2012. The sample selection is based on purposive sampling method with the purpose of obtaining a representative sample in accordance with the specified criteria. Banking criteria sampled in this study are:
1) Included in this type of banking companies listed in Indonesia Stock Exchange during the period 2007-2012.
2) All data required for this study is available to complete.

Based on the sample above criteria, the obtained 19 (nineteen) banking as the study sample. The unit of analyisis of this study is the banking companies listed in Indonesia Stock Exchange in 2007-2012. According to the data, there are 35 companies.

Results and discussion

Using multiple linear regression method, to test the effect of the independent variable dependent variable tehadap produced the coefficient of determination, the value of the F test and t test values as presented in Table 1, Table 2 and Table-3.

Table-1

Results Coefficient of Determint Model Summaryb

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.870[a]	.758	.741	5.20558

a. Predictors: (Constant), $JDKI_t$, JKA_t, $JKPR_t$, KTA_t, LDR_t, ROE_{t-1}

b. Dependent Variable: ROE_t

From Table-1 above the model summary magnitude adjusted R2 is 0.741, which means 74.10% return on equity variation can be explained by the variation of the independent variables to five independent board, audit committee, risk monitoring committee, the increase in total assets, and loan to deposit ratio. While the remaining 25.90% is explained by other causes outside the model.

Tabel-2

Test of Simultan

ANOVA[b]

Model		F	Sig.
1	Regression	45.875	.000[a]
	Residual		
	Total		

a. Predictors: (Constant), $JDKI_t$, JKA_t, $JKPR_t$, KTA_t, LDR_t, ROE_{t-1}

b. Dependent Variable: ROE_t

From the above obtained ANOVA calculated F value of 45 875 with probability 0.000. Because the probability is much smaller than 0.05, the regression model can be used to predict the return on equity, or it can be said that the independent board, audit committee, risk monitoring committee, the increase in total assets, loan to deposit ratio and return on equity last year in together / simultaneously have a significant impact on the financial performance of banks.

Tabel-3

Output partial analys

Coefficients[a]

Koef. Determinasi	t hitung	Sig.
8.028	2.004	.048
-.027	-.033	.974
.385	.583	.561
-.424	-.778	.439
.112	2.734	.008
-.047	-.903	.369
.669	8.383	.000

a. Dependent Variable: ROE_t

Some of the independent variables included in the regression model variables independent board, audit committee, risk monitoring committee, the increase in total assets, loan to deposit ratio and return on equity last year, only the increase in total assets and return on equity last year that have a significant effect, this can be seen from the significant probability for these variables is smaller than 0.05.

Based on the above table 3, can be explained in detail as follows:
1) Constants of 8028 states that if the independent variables are considered constant, then the average value is equal to 802.8% ROEt.
2) The value of the coefficient of -0027 on the probability JDKIt significantly by 0974 (greater than 0.05) shows that the number of independent board no significant effect on the financial performance of banks. This is consistent with previous research that states that the more the number of independent board have a negative impact on the performance of the company. However, the impact of the independence of the board of directors on the financial performance of this company still produces a variety of conclusions.
3) JKAt significant probability value of 0561 (greater than 0.05) shows that the number of audit committee no significant effect on the financial performance of banks. This is in line with several previous studies that stated that there was no significant correlation between the value of the company (ROE) of the size of the board and the board's audit committee.
4) Value of 0439 JKPRt significant probability (greater than 0.05) shows that the number of risk monitoring committee has no significant effect on the financial performance of banks.
5) Coefficient KTAt of 0112 at a significant probability of 0.008 (less than 0.05) shows that the increase in total assets has positive influence on the financial performance of banks.
6) Value of 0369 LDRt significant probability (greater than 0.05) shows that the loan-to-deposit ratio has no significant effect on the financial performance of banks.
7) Coefficient ROEt-1 by 0669 at a significant probability of 0000 (less than 0.05) shows that the return on equity last year a positive effect on the financial performance of banks.

Conclusions and recommendations

This research generally aims to identify and provide empirical evidence that good corporate governance and bank fundamental effect on the financial performance of banks. The results show that good corporate governance by the number of independent board, audit committee and risk monitoring committee and bank fundamentals are represented by the increase in total assets, loan to deposit ratio and return on equity last year together /simultaneous effect on the financial performance of banks.

The results of the second test showed that of the six indicators of independent board, audit committee, risk monitoring committee, the increase in total assets, loan to deposit ratio and return on equity last year, which proved to be partially significant effect on the financial performance of banks only increase in total assets and return on equity last year.

The research results can be briefly described as follows: 1) The number of independent board (JDKIt) no significant effect on the bank's financial performance, 2) The number of audit committee (JKAt) no significant effect on the financial performance of banks, 3) Total Risk Monitoring Committee (JKPRt) no significant effect on the financial performance of banks, 4) The increase in total assets (KTAt) positive significant effect on the financial performance of banks, 5) Loan to deposit ratio (LDRt) no significant effect on the financial performance of banks, 6) Return on equity last year (ROEt-1) positive significant effect on the financial performance of banks.

Given the bank has a major role in driving economic growth in Indonesia, then good corporate governance is essential applied in the banking world, which in turn can improve the performance of banks.

The number of independent board and committee monitors the risks are almost the same in each year is thought to be a factor that causes the indicators of good corporate governance did not significantly affect the financial performance of banks. Investors and prospective investors should be cautious in making business decisions, not only focused on profit information, but also consider the non-financial information, such as the existence of the company's internal mechanisms.

This study has the limitations of the data that can not optimally describe the condition of the banking sector in Indonesia. In future studies can be tested back on the same issue is to: 1) Increase the number of samples, the samples used in this study have not been able to enter the entire banking companies because of limited information obtained. With a larger sample study results are expected to provide a more concrete so that research becomes more precise and accurate, 2) Insert the other variables as independent variables, variables institutional ownership and possession of the directors. Institutions such as insurance companies, pension funds with a large portion of ownership can press management to work in the best interests of shareholders. Likewise, a large portion of ownership of the members of the board of directors, and 3) In a subsequent study, the audit committee variables should be eliminated because it is based on the results of the study and some previous studies showed that the number of audit committee no significant effect on the financial performance of the company.

References

Adriani, Irma. 2011. Effect of Investment Opportunity Set and Corporate Governance Mechanism on the Quality of Earnings and Value. Thesis Strata-I, Faculty of Economics, University of Diponegoro, Semarang.

Aras, Guler. 2008, Governance and sustainability: An investigation into the relationship between corporate governance and corporate sustainability. Journal of Management decision.

Aryani, Etha Rizki. 2011. Effect of Good Corporate Governance and Ownership Structure Against Agency Cost. Thesis Strata-I, Faculty of Economics, University of Diponegoro, Semarang.

Bushman, Robert M, 2003. Transparency, financial accounting information, and

Falah, Mohammad Fajrul. 2011. Analysis of Internet-Based Corporate Governance Disclosure by Public Companies in Indonesia in 2010. Thesis Strata-I, Faculty of Economics, University of Diponegoro, Semarang.

Eldomiaty,Tarek Ibrahim, Chong Ju Choi, (2006) "Corporate governance and strategic transparency: East Asia in the international business systems", Corporate Governance: The international journal of business in society, Vol. 6

Ghozali, Imam. 2009. Applications Multivariate Analysis With SPSS program. Agency Publisher University of Diponegoro, Semarang.

Herman. 2011. Effect of Good Corporate Governance Against Earning Management. Blogg mess, University of Banda Aceh.

Jogiyanto. 2004. Business Research Methodology: One Kaprah and Experiences. 2004/2005 edition. London: BPFE.

Laila Noor. 2011. Analysis of Effect of Good Corporate Governance Against Corporate Value. Thesis Strata-I, Faculty of Economics, University of Diponegoro, Semarang.

Lestari, Ekowati Dyah. 2011. Influence of Corporate Governance Against Financial Performance. Thesis Strata-I, Faculty of Economics, University of Diponegoro, Semarang.

Nasution, Marihot and Doddy Setiawan. 2007. Influence of Corporate Governance Against Profit Management in Banking Industry in Indonesia. National Symposium on Accounting X UNHAS Makassar 26-28 July 2007.

Panggabean, Ryan Raymond. 2011. Influence of Corporate Governance Practices Against Profit Management Companies Go Public In in Indonesia. Thesis Strata-I, Faculty of Economics, University of Diponegoro, Semarang.

Prasetyo, Wika Septian. 2011. Influence of Corporate Governance, Bonus, Plans, Debtcovenant, and Firm Size Of Earnings Management. Thesis Strata-I, Faculty of Economics, University of Diponegoro, Semarang.

Romano, Roberta, 2001, Making of institutional investor activism a valuable mechanism of corporate governance, Yale Journal on Regulation

Piscula, Thomas, J. 2011. Governance and Merger Activity in Banking, Journal of business and economic studies