

Corporate Governance and Profitability: The Case of Corporate Governance Index Firms in Indonesia

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The main objective of the current study is to investigate the impact of corporate governance on the profitability of Indonesian firms. Particularly, the study has focused on the good corporate governance practices on the profitability of firms listed in the Indonesian stock exchange. The panel data methodology is employed in the study, and the data of 21 firms over the period of five years from 2014 to 2018 is gathered from the annual audited account of Indonesian listed firm. Different diagnostic test is used to trace the appropriate panel estimates and basing on the Hausman test the random effect estimates appears as a most suitable estimates for the set of data we have employed. The findings of the study are providing support to the proposed hypothesis that the good corporate governance improve the performance of the Indonesian firms. The findings of the study will be helpful for the policymakers and practitioners in understanding the issues related to the good corporate governance practices in Indonesia. It is hoped that with good management rights and responsibilities will be distributed among shareholders. Going concern is the identified goal of a series of GCG practices. The study is of the view that sustainability of a company is determined by the implementation of good corporate governance.

Keywords: *Corporate Governance, profitability, Indonesia*

Introduction

Economic development in Indonesia continues to grow and Indonesia must continue to compete with current global conditions. The number of emerging foreign companies in Indonesia proves that Indonesia is a potentially influential country. The term Good Corporate Governance, hereinafter abbreviated as GCG, is no stranger. GCG is a system and structure for

managing companies with the aim of increasing shareholder value and allocating various parties with interests in the company (stakeholders) such as creditors, suppliers, business associations, consumers, workers, the government and the wider community (Tangkilisan, 2003:11). This is major interest to any company as a universal goal is to implement good governance (GCG) so as to have a 'going concern' in the marketplace.

The fact that they are not yet institutionalized as a whole is one of the problems experienced by banks in the banking sector, this shows the absence of oversight of exceedances and or violations of Batas Minimum Pemberian Kredit (BMPK) (Saudi et al., 2019; Hidhiir et al., 2019). In accordance with this, every company must implement corporate governance properly to maintain its long-term survival. In the implementation of good GCG transparency is crucial to build a strong corporate fundamental (Sinaga et al., 2019; Basheer et al., 2018). Corporate governance is bank governance that applies the principles of transparency, accountability, responsibility, independence, and fairness. With good corporate governance, the company is expected to improve company performance and company profitability.

This is reinforced by Grace (2018: 3) in his research who states that corporate governance is seen as a system where organizations are well managed, goals are set and achieved, risks are monitored and assessed and performance is improved in a better direction (Hamilton, 2003). It is hoped that with good management rights and responsibilities will be distributed among shareholders. Going concern is the identified goal of a series of GCG practices. The sustainability of a company is determined by the implementation of good corporate governance.

Hanafi and Halim (2012: 85) explain that sales revenue measured by a ratio is called the profitability ratio. The ratio of Return on assets (ROA) and Net Interest Margin (NIM) is used as a proxy for the independent variable. Often Return on assets (ROA) is referred to as return on investment because Return On Assets looks at the extent to which the investment is able to provide returns as expected and the investment is actually the same as the invested or placed company assets. A management's ability to manage to earn assets to generate interest income from activities on bank operations is called the Net Interest Margin (NIM). Therefore, good corporate governance is needed in order to fulfil all rights for all stakeholders and avoid agency conflicts.

The implementation of GCG in Indonesia is currently relatively lagging behind compared to countries in the ASEAN region. OJK Board of Commissioners Chairman Wimbuh Santoso revealed in CNN Indonesia, 2017 by only two issuers from Indonesia who managed to enter the list of the 50 best issuers in the 2015 ASEAN Corporate Governance Awards held by the ASEAN Capital Markets Forum in AC Manila. The two issuers are PT Bank Danamon Tbk and PT Bank CIMB Niaga Tbk. The awarding of the ASEAN Corporate Governance Award

organized by the ASEAN Capital Markets Forum (ACMF) is held once a year, involving 6 countries: Indonesia, Malaysia, Philippines, Singapore, Thailand, and Vietnam.

At the 2015 ASEAN Corporate Social Award, Indonesia was awarded the Top 2 (two) Publicly Listed Companies with Outstanding Achievement by the Country namely PT Bank Nisp Tbk and PT Bank Tabungan Negara Tbk and Top 3 Publicly Listed Companies by Country, namely Aneka Tambang Persero, PT Bank Cimb Niaga, and PT Bank Danamon Indonesia. This is different from the assessment conducted by the Indonesian Institute for Corporate Governance (IICG) in their research program and the ranking of the Corporate Governance Perception Index (CGPI) throughout 2014-2018 explaining that banks that enter the assessment conducted by IICG, namely, BCA, Mandiri, BTN, OCBC NISP, BRI, Permata, BNI, and BJB including valuation with a highly trusted category with high GCG scores. In contrast, Bank Cimb Niaga and Bank Danamon Indonesia which won the award in the 2015 ASEAN Corporate Governance Award did not receive an assessment from IICG.

This study uses independent variables, namely GCG which is proxied using Composite Values issued by the Indonesian Institute for Corporate Governance (IICG) while the dependent variables are ROA and NIM (Hussain et al., 2019). The calculation formula for ROA and NIM used is:

$$\frac{\text{Laba Sebelum Pajak}}{\text{Total Assets}} \times 100\%$$

(Syamsuddin, 2009)

$$\frac{\text{Pendapatan Bunga Bersih}}{\text{Rata-rata aset produktif}} \times 100\%$$

(Pandia, 2012)

H₁: Good Corporate Governance has a significant influence on Return On Assets (ROA)

H₂: Good Corporate Governance has a significant influence on *Net Interest Margin* (NIM)

Methodology

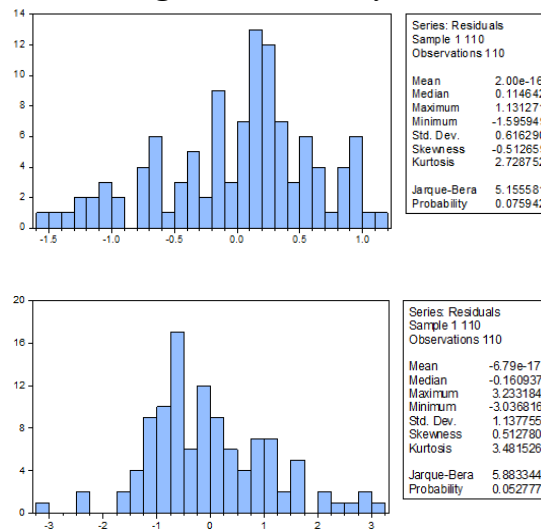
The research method used in this study is a quantitative approach, which is a method for testing certain theories by examining relationships between variables. These variables are measured first so that data consisting of numbers can be analyzed based on statistical procedures (Noor, 2011: 38; Rismayadi & Maemunah, 2018). The study sample used Purposive Sampling techniques which contained 22 selected companies and used banking company time series data listed on the Indonesia Stock Exchange (IDX) in the 2014-2018 period.

Table 1: Sample Research

| No | Kode | Nama Perusahaan |
|----|------|--|
| 1 | BBCA | Bank Central Asia Tbk. |
| 2 | BBKP | Bank Bukopin Tbk. |
| 3 | BBNI | Bank Negara Indonesia Persero Tbk. |
| 4 | BBNP | Bank Nusantara Parahyangan Tbk. |
| 5 | BBRI | Bank Rakyat Indonesia Persero Tbk. |
| 6 | BBTN | Bank Tabungan Negara Persero Tbk. |
| 7 | BINA | Bank Ina Perdana Tbk. |
| 8 | BJBR | Bpd Jawa Barat dan Banten Tbk. |
| 9 | BMAS | Bank Maspion Indonesia Tbk. |
| 10 | BMRI | Bank Mandiri Persero Tbk. |
| 11 | BNBA | Bank Bumi Arta Tbk. |
| 12 | BNGA | Bank Cimb Niaga Tbk. |
| 13 | BSIM | Bank Sinarmas Tbk. |
| 14 | INPC | Bank Arta Graha Internasional Tbk. |
| 15 | MAYA | Bank Mayapada Internasional Tbk. |
| 16 | MCOR | Bank Cina Construction Bank Indonesia Tbk. |
| 17 | MEGA | Bank Mega Tbk. |
| 18 | NAGA | Bank Mitra Niaga Tbk. |
| 19 | NISP | Bank OCBC NISP Tbk. |
| 20 | NOBU | Bank Notionanobu Tbk. |
| 21 | PNBN | Bank Pan Indonesia Tbk. |
| 22 | SDRA | Bank Wori Sodara Indonesia 1960 Tbk. |

Conclusions & Implications

Figure 1. Normality test



Data Analysis Model

Based on the results of processing using Random Effect Model panel data regression are:

$$ROA = -3,380 + 1,893GCG + e$$

$$NIM = 2,537 + 1,340GCG + e$$

The negative constant value for ROA shows that the dependent variable Y will decrease constantly if the other variables, namely GCG, are zero. The results of this study are in line with the research conducted by Putra (2017: 107-108) and overall for the Y variable that ROA on Corporate Governance has a significant effect.

Adjusted R-Squared value in this study was 48.8%. This shows that the implementation of Good Corporate Governance (GCG) contributes to Return on Assets of 48.8% while the remaining 51.2% is a contribution from other variables not examined. The coefficient value of the implementation of Good Corporate Governance (GCG) contributes to Net Interest Margin by 19.8% while the remaining 80.2% is contributed by other variables not examined.

This study is in line with Grace et al (2018: 11) that the application of good governance will automatically improve company performance. The research data taken is one of them is banking in Kenya. In addition, research according to Dwi et al (2018: 85) and Tjondro (2011: 14) shows the same results, namely a positive effect between GCG and ROA. The results of this study are also in line with those carried out by Widiamsa (2017: 15) regarding GCG towards NIM having a positive influence.

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