

The Influence of Good Corporate Governance on the Financial Performance of Banking Companies Listed on the Indonesia Stock Exchange

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ABSTRACT

This study investigates the impact of Good Corporate Governance (GCG) components— independent commissioners, institutional ownership, managerial ownership, and audit committees—on the financial performance of banking subsector companies listed on the Indonesia Stock Exchange from 2018 to 2023. Using quantitative analysis of secondary data, the findings reveal that independent commissioners positively influence financial performance, while both institutional and managerial ownership negatively affect it. Conversely, the audit committee does not significantly impact financial performance. The study highlights the importance of governance structures in enhancing financial outcomes and recommends focusing on board composition and ownership structures for improved performance.

INTRODUCTION

Good Corporate Governance (GCG) is fundamentally a framework that governs the structure of a corporation, delineating roles, authority, and responsibilities among its various components. According to the General Guidelines for Good Corporate Governance in Indonesia, issued by the National Committee on Governance Policy (KNKG) in 2006, five fundamental principles guide the implementation of GCG: transparency, accountability, responsibility, independence, and fairness and equality. GCG establishes a structure that facilitates the determination of a company's vision and mission and serves as a means for selecting performance monitoring techniques. It assures stakeholders that their investments will be safeguarded against misappropriation by corporate managers.

In the banking sector, effective GCG mechanisms are crucial for enhancing financial performance, as adherence to established governance principles positively correlates with financial outcomes. Two essential aspects of balance must be maintained for successful GCG: internal balance, which entails providing useful information for performance evaluation, resource management, internal transactions, and management decision-making; and external balance, which involves delivering business information to shareholders, creditors, banks, and other relevant stakeholders (Manossoh, 2016).

The current competitive business landscape requires companies to continuously innovate, improve performance, and balance potential risks to remain viable (Sulistiyowati & Fidiana, 2017). A significant vulnerability among Indonesian firms is the inadequate implementation of GCG principles. The banking sector, due to its unique nature and business characteristics, is particularly susceptible. Wijaya (2002) notes that banks must adhere to three fundamental tenets: trust, compliance, and prudence. However, the execution of GCG within banking institutions has faced numerous obstacles. The Indonesian Institute for Corporate Governance's GCG Perception Index 2003 revealed that compliance is often merely regulatory, rather than a result of genuine commitment to GCG principles.

Additionally, effective GCG practices necessitate the commitment of the board of commissioners, functional committees, and management to provide transparent communication to shareholders and stakeholders. The banking sector is heavily regulated and supervised by the Financial Services Authority (OJK), emphasizing prudent operational practices. Since 1991, Bank Indonesia has implemented various regulations to promote GCG among banks. However, many banks continue to struggle with compliance due to factors like a lack of professional independence in leadership and excessive owner intervention, leading to issues like violations of the Maximum Limit of Credit Distribution (BMPK).

Numerous cases in the banking sector highlight these challenges. According to data from databoks.katadata.co.id on January 10, 2024, the OJK reported that 23,064 complaints regarding banking issues were lodged by the public in 2023. Complaints primarily revolved around credit restructuring and

financial information systems. Furthermore, the Deposit Insurance Corporation (LPS) noted that from 2005 to 2023, 122 banks went bankrupt, with a significant number being rural banks (BPR). Fraud cases, such as the issuance of fake deposit slips by employees of PT Bank Negara Indonesia (BNI) and credit card fraud involving PT Bank Rakyat Indonesia (BRI), further underscore the need for robust GCG practices.

To effectively implement GCG, it is essential to clarify the roles and responsibilities of internal stakeholders, particularly through robust internal control systems that guide, supervise, and assess company resources. The KNKG (2006) emphasizes that achieving long-term success through GCG requires high integrity, necessitating ethical guidelines that shape corporate behavior. This study will focus on key internal elements of GCG, including independent commissioners, institutional ownership, managerial ownership, and audit committees.

Independent commissioners are vital for ensuring objective oversight of management, reducing the likelihood of financial misreporting. According to FCGI (2002), independent commissioners serve two primary functions: advisory support and management oversight, thereby balancing the interests of investors and management. Institutional ownership, representing shares held by entities like investment firms and banks, enhances managerial performance oversight and mitigates earnings management practices (Endang, 2018; Wiranata & Nugrahanti, 2013). Managerial ownership, where managers also hold company shares, aligns managers' interests with those of shareholders, minimizing agency conflicts (Jensen & Meckling, 1976).

Moreover, audit committees play a crucial role in maintaining the credibility of financial reports, acting as intermediaries between shareholders and management (Honi et al., 2020). The impact of GCG on financial performance has garnered attention since the financial crisis in Indonesia in 1997, prompting significant reforms in banking practices. Financial performance is often assessed through financial ratios, with Return on Assets (ROA) serving as a key indicator of a company's efficiency in generating earnings from its assets. Historical data indicates fluctuations in ROA for Indonesian banks between 2018 and 2023, reflecting the ongoing need for improved GCG practices.

Prior studies have revealed varying effects of GCG components on financial performance. For instance, Okto & Iwan (2020) found a positive relationship between independent commissioners and financial performance, while Sofianti (2022) reported a negative, insignificant effect. Similarly, while Shinta, Mumun, & Carolyn (2023) identified a positive impact of institutional ownership, Ariyani & Djoko (2022) found it to be negatively significant. The influence of managerial ownership on financial performance has also yielded mixed results in various studies. Given these research gaps, this study aims to explore the impact of GCG on the financial performance of banking subsectors listed on the Indonesia Stock Exchange, focusing on independent commissioners, institutional ownership, managerial ownership, and audit committees.

LITERATURE REVIEW

1. Good Corporate Governance

Good Corporate Governance (GCG) refers to a system that regulates corporate management to create added value for stakeholders. It ensures the rights of shareholders to receive accurate and timely information while companies are obligated to disclose performance details transparently (KNKG, 2006). GCG principles include transparency, accountability, responsibility, independence, and fairness (Manossoh, 2016). Implementing GCG aims to enhance corporate performance, protect investors, and ensure professional management (FCGI, 2012). GCG structures and mechanisms, involving boards of commissioners and audit committees, are vital for effective management and oversight (Arifin & Chariri, 2011).

2. Financial Performance

Financial performance, according to Irham Fahmi (2020), is an analysis to assess how well a company follows financial management rules. It provides an overview of a company's financial status by analysing specific tools to evaluate performance over time. Srimindarti (2006) notes that financial performance assessment helps determine operational effectiveness and company efficiency. One key metric used is Return on Assets (ROA), which reflects profitability by showing how assets contribute to profit generation (Harmono, 2016). Financial analysis methods include trend analysis, ratio analysis, and cash flow analysis, offering insights into a company's financial condition (Jumingan, 2011).

3. Characteristics of Banking Companies

Banks, as defined by PSAK No. 31, are financial intermediaries that facilitate fund transfers between savers and borrowers, while supporting payment systems. Indonesian Law No. 10 of 1998 describes a bank as a business entity that collects public deposits and extends credit to improve societal welfare. Banks face stricter regulations, such as the Capital Adequacy Ratio (CAR) requirement. Bank Indonesia evaluates a bank's health through financial reports, crucial for maintaining investor trust and avoiding profit manipulation issues. Types of banks in Indonesia include government-owned, private, foreign, mixed-ownership, and cooperative banks.

METHODOLOGY

1. Type of Research and Data Collection Method

This quantitative research utilizes secondary data, collected through documentation from financial reports of banking subsector companies listed on the Indonesia Stock Exchange (2018-2023). Data is sourced from official company websites and www.idx.co.id, as well as articles and journals, to test theories statistically through variable analysis.

2. Research Population and Sample

The population in this study consists of banking sector companies listed on the Indonesia Stock Exchange (IDX) from 2018 to 2022, totalling 57 companies (Sugiyono, 2018). The sample is selected using purposive sampling,

based on specific criteria such as having complete data on independent boards, institutional ownership, managerial ownership, and audit committees. After excluding companies that don't meet these criteria, 21 companies are included, resulting in a total of 126 observations over six years (Sugiyono, 2016). The data is sourced from the IDX website and processed by the researcher.

3. Variable Measurement and Operational Definition

This study examines the financial performance of companies (Y) as the dependent variable, measured using Return on Assets (ROA), which is calculated as net income divided by total assets (Fahmi, 2014; Harahap, 2010). The independent variables include the Independent Board of Commissioners (X1), measured as the ratio of independent commissioners to total commissioners, Institutional Ownership (X2), which is the percentage of shares held by institutions, Managerial Ownership (X3), the percentage of shares held by management, and Audit Committee (X4), assessed by the total number of audit committee members, emphasizing the importance of good governance (Lestari & Cahyonowati, 2013; Kustina Ambar, 2019; Budiarti & Sulistyowati, 2014).

4. Data Analysis Method

The data analysis method comprises descriptive statistics and panel regression. Descriptive statistics, according to Sugiyono (2018) and Ghozali (2018), summarizes data by examining minimum, maximum, mean, standard deviation, skewness, and kurtosis, indicating normal distribution when skewness and kurtosis are within -2 to 2. The panel regression model combines time series and cross-sectional data from 21 banking companies listed on the Indonesia Stock Exchange from 2018-2023 (Basuki & Prawoto, 2017). Model selection involves Chow, Hausman, and Lagrange Multiplier tests to determine the most suitable estimation approach between Common Effect, Fixed Effect, and Random Effect models.

5. Hypothesis Testing

The hypothesis testing includes T-test, F-test, and coefficient of determination. The T-test assesses the influence of individual independent variables on the dependent variable, using a significance level of 5% (Ghozali, 2017). The F-test evaluates the collective impact of independent variables (Ghozali, 2017). The coefficient of determination (R^2) measures the model's explanatory power for the dependent variable, with adjusted R^2 used to account for the number of independent variables (Ghozali, 2018).

RESULTS AND DISCUSSION

1. Descriptive Statistics

Table 1. Descriptive Statistics Result

	N	Minimum	Maximum	Mean	Std. Deviation
Financial performance	114	0.000	0.035	0.013	0.008
Independent Board of Commissioners	114	0.170	0.800	0.511	0.148
Institutional Ownership	114	0.445	1.000	0.824	0.159
Managerial Ownership	114	0.000	0.193	0.017	0.037
Audit Committee	114	2.000	8.000	4.140	1.425

Descriptive statistical analysis summarizes collected data without generalizing results (Sugiyono, 2018). Using EViews 12, 114 observations were analysed. Financial performance (mean: 0.013, SD: 0.008) shows homogeneity; independent commissioners (mean: 0.511, SD: 0.148) and institutional ownership (mean: 0.824, SD: 0.159) also demonstrate similar patterns. In contrast, managerial ownership (mean: 0.017, SD: 0.037) reveals heterogeneity. Audit committees (mean: 4.14, SD: 1.425) show homogeneity. Overall, independent commissioners and institutional ownership indicate stable data distribution, while managerial ownership reflects variability, impacting performance metrics (Ghozali, 2018; EViews 12, data processed, 2024).

2. Partial Test (T-Test)

The partial test (T-test) assesses the influence of independent variables on the financial performance of banking subsector companies listed on the Indonesia Stock Exchange using the Random Effect Model.

Table 2. Partial Test Result

Hypothesis	Variables	Prob.	Conclusion
Hypothesis 1	Independent Board of Commissioners	0.0469	H1 accepted
Hypothesis 2	Institutional Ownership	0.0000	H2 accepted
Hypothesis 3	Managerial Ownership	0.0004	H3 accepted
Hypothesis 4	Audit Committee	0.4489	H4 rejected

The results indicate that the Independent Board of Commissioners positively influences financial performance, as shown by a probability value of 0.0469 ($p < 0.05$) and a t-statistic of 2.0101. Institutional Ownership negatively impacts financial performance with a probability of 0.0000 and a t-statistic of -4.5150. Managerial Ownership also negatively influences financial performance, with a probability of 0.0004 and a t-statistic of -3.6782. However, the Audit Committee does not significantly affect financial performance, as the probability value is 0.4489 ($p > 0.05$) and the t-statistic is -0.7599.

3. Simultaneous Test (F-Test)

The simultaneous test (F-test) is used to demonstrate the combined effect of independent variables on the dependent variable. In this study, the F-test assesses whether the Independent Board of Commissioners, Institutional Ownership, Managerial Ownership, and the Audit Committee collectively influence changes in financial performance. Based on the Random Effect Model, the test results show a Prob(F-statistic) value of 0.000057, which is less than 0.05, indicating that these independent variables significantly influence the financial performance of companies in the banking subsector simultaneously.

4. Coefficient of Determination Test (R²)

The coefficient of determination (R²) test measures the extent to which independent variables (X) explain the variation in the dependent variable (Y) as a percentage. Based on the Random Effect Model, the Adjusted R² value is 0.172, indicating that the Independent Board of Commissioners, Institutional Ownership, Managerial Ownership, and the Audit Committee collectively explain 17.2% of the variation in financial performance. This means that 82.8% of the variation in financial performance is influenced by other factors not included in this study.

5. The Influence of Independent Board of Commissioners on Company Financial Performance

The hypothesis testing results indicate that the Independent Board of Commissioners has a positive impact on the financial performance of banking subsector companies listed on the Indonesia Stock Exchange, supporting H1. This aligns with the findings of Okto & Iwan (2020). The presence of independent commissioners not only fulfils regulatory requirements but also strengthens corporate oversight, leading to improved financial performance. By acting objectively and impartially, independent commissioners enhance transparency, promote good corporate governance, and make more accurate decisions. This, in turn, boosts investor and stakeholder confidence, improves the quality of financial reporting, and helps prevent fraud, ultimately supporting the company's goal of enhancing financial performance.

6. The Influence of Institutional Ownership on Company Financial Performance

The hypothesis testing results indicate that institutional ownership negatively affects the financial performance of banking subsector companies listed on the Indonesia Stock Exchange, supporting H2. This is consistent with Ariyani & Djoko (2022), who found a significant negative impact of institutional ownership on company performance. Institutional ownership often leads to heightened oversight, as large institutional shareholders exercise substantial control over management, which can result in excessive pressure, limiting managerial flexibility and innovation in executing long-term strategies. Over-reliance on institutional investors may also prioritize short-term gains over

long-term growth, creating potential conflicts. Therefore, companies should enhance communication with institutional shareholders, promote long-term investment policies, and maintain a balance between shareholder interests and corporate goals.

7. The Influence of Managerial Ownership on Company Financial Performance

The hypothesis testing results reveal that managerial ownership negatively impacts the financial performance of banking subsector companies listed on the Indonesia Stock Exchange, thus supporting H3. This finding aligns with research by Eliessye et al. (2019), which indicates that managerial ownership has a negative and insignificant effect on corporate financial performance. Managerial ownership can mitigate agency problems by aligning managers' interests with those of stakeholders, particularly when the proportion of shares held by managers and directors increases, which can decrease tendencies for manipulation (Purwanto, Bustaram, Subhan, & Risal, 2020). However, managers with substantial ownership may adopt a conservative approach to decision-making, avoiding risks necessary for long-term growth. Additionally, they may become too powerful, making oversight by the board or other shareholders challenging. Therefore, it is advisable for companies to establish robust oversight mechanisms to ensure managerial accountability, balance managerial ownership with the interests of other shareholders, and promote policies that support long-term beneficial decisions for the company.

8. The Influence of Audit Committee on Company Financial Performance

The hypothesis testing results indicate that the audit committee does not affect the financial performance of banking subsector companies listed on the Indonesia Stock Exchange, leading to the rejection of H4. This finding is consistent with Syafira et al. (2023), who found that the audit committee has no significant impact on financial performance. This implies that an increase in the number of audit committee members does not necessarily enhance financial performance; in fact, the mere presence of three members may only satisfy the minimum requirement without ensuring effective oversight. The presence of an audit committee could slow decision-making processes, negatively affecting the company's responsiveness to market changes. Additionally, maintaining an effective audit committee requires additional resources for training and compensation, potentially diminishing profitability. The effectiveness of the audit committee largely depends on the quality and independence of its members; if they lack adequate experience, their presence may be ineffective. Moreover, companies with numerous audit committees may face "overregulation," hindering innovation and flexibility.

CONCLUSIONS AND RECOMMENDATIONS

This study aims to examine the influence of independent commissioners, institutional ownership, managerial ownership, and audit committees on the financial performance of companies, both simultaneously and partially. The findings indicate that independent commissioners positively impact the financial performance of firms, while institutional ownership and managerial ownership both exert a negative influence. In contrast, audit committees do not affect the financial performance of the companies. Therefore, it is recommended that companies pay attention to the composition of the board of commissioners, as well as institutional and managerial ownership, to enhance financial performance.

FURTHER STUDY

Future research on the influence of independent commissioners, institutional ownership, managerial ownership, and audit committees on the financial performance of banking companies could explore additional variables like corporate social responsibility and board diversity. Comparative analyses across different industries or countries could provide broader insights. Longitudinal studies may reveal changes over time, while qualitative research could uncover decision-making processes within governance structures. Investigating the impact of external economic conditions, technological advancements, and regulatory changes on financial performance can further enhance understanding. These approaches will contribute to more effective governance practices and improved financial outcomes in the banking sector.

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