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Impact of Good Corporate Governance Implementation and Risk Management on Bank Performance and Corporate Values

Tyahya Whisnu Hendratni [1]
[1] *Faculty of Economy and Business, Universitas Pancasila*
Corresponding Author: Tyahya Whisnu Hendratni

Abstract: *Monetary and real sectors are economic activities that have developed dynamically. One of the effects is towards the banking sector. The purpose of this study is to determine between good corporate governance (GCG) and risk management and its implementation with bank performance before and after the implementation of OJK regulation based on the test conducted. This study also assesses the company (bank) is an approach used to see all the needs and information related to the corporate value (bank) that can be prepared completely by policymakers. This research method uses explanative survey with structural equation modeling analysis. The sample of this research is foreign, government, and private banks which can be obtained from Bank Indonesia (BI) website. The period taken is the period 2008 - 2016. The role of the financial services authority affects the average value of GCG and risk management mechanisms. However, the performance of the bank and the value of the company has no effect when compared before and after the formation of the financial services authority.*

Keywords*: GCG, risk management, corporate value, bank performance*

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I. Introduction

Business banking is a business that has its own risks. Therefore, there is a need to have risk management which is an excellent core in order to survive and provide profitable sustainability. The institution that manages banks in each country and several international institutions. Organization for Economic Corporation and Development (OECD) and Bank for international settlements (BIS) have issued various statements on the important for GCG to create the operating procedure. In addition, empirical research examines GCG implementation and risk management application, investigate the impact on the implementation for the banks and determine the factors GCG implementation [1].

Bank as an institution has a vital role for economic and social [2]. Regulators of banking management were generally caused by the weaknesses of GCG and risk management implementation. It does not only impact the bank institutions, but also the wider community who put their funds in banks which cause systemic risks to other banks [3]. Besides that, loss of public trust to the bank which causes disruption to banking stability [4].

GCG influences the trust among the governments, societies and private sectors due to the principles of transparency, accountability, and participation. The involvement of stakeholders and citizenry in the business world are the necessary requirements to make the policy implementation successful. The decision of the policy implementation decides by the power possessed, however, it also depends on the actors involved [4].

Banks as financial services have a significant role for receive, store, transfer, pay, exchange, lend, invest or protect money for consumer benefit. For Indonesian banks, credit is the main asset to generate interest income other than treasury assets and fee-based income. Due to that, credit has an important and strategic role [4].

The inability of companies to survive is the simplest way to indicate company failure in producing a good performance. The advocates of stakeholders approach have been emphasized that the survival company is not only the interests of the owner of the company, but it is also the main concerns of the stakeholders involved. In the banking context, bank failure does not only affect the owners or shareholders of the bank, but it also affects the wider community on depositing their funds. It also gave impact on the systemic risks for other banks. The failure of the bank can eliminate the trust of the public in the banking system that will impact disrupted the economic system [5].

The aspects of risk management in the business financial intermediary and participants in the payment system contain a variety of risks. There are various regulations governing the bank's authority to apply the bank prudential regulation for business operation. It includes the principles of sound credit, the lack of obligation to provide capital, the obligation to maintain liquidity, and special regulations that must be obeyed by every public bank regarding risk management [5].

Internal auditors are one of the pillars of organizational governance who assess the effectiveness of risk management, control, and organizational governance. [6] In the United States throughout 2009, 140 banks were declared failed and closed and then in the first two months of 2010, there were 25 banks closed again. The financial crisis made the government pay for consumer protection. The budget that comes out as protection for customers is valued at USD 252 million. This fee must be borne in order to prevent loss of trust in the banking system.

The researchers believe that GCG corporate governance, risk management, and compliance are the actual management aspect that is not new to business practitioners and academics. However, GCG and risk management have increasingly become a concern since the early 2000s, especially after the banking crisis that hit several countries in Asia including Indonesia in the 1990s specifically in 1997-1998. There were 16 banks were liquidated on 1st November 1997 and the government determined seven banks were frozen their operations and seven other banks were taken over (Bank Take Over (BTO)) on 3 April 1998. Beginning in August 1998, three BTO banks were frozen due to the deteriorating condition of several BTOs, however, the banking system in Indonesia still continued. Then, 38 banks were frozen to close on 13 March 1999. Furthermore, as a rescue strategy, the Government recapitalized six banks who belonged to the central government and 12 regional banks who belonged to the local government.

The influence of GCG towards the company is one of the vital factors that influence the company's strategy [7]. The governance perspective approach examines that company as a set of governance alternative [8]. GCG basically is a set of business systems, commissioners, shareholders, and other stakeholders that form the structure and achieve company goals [9].

This study focuses on GCG implementation to the banks in order to achieve bank goals that measure by using the bank performance. In this study, GCG and risk management implementation were reviewed for the impacts on bank performance. With a multiple stakeholders approach, this study analyzes the effect of GCG implementation and risk management implementation on bank performance from the owner's perceptions and from the regulator's perceptions. The regulator serves to protect the interests of stakeholders who are not bank owners, and regulators are external factors that encourage the implementation of GCG and the implementation of bank risk management. Besides that, considering the owner has the right to determine the profit allocation, the GCG implementation assumption can relate to the owner's objectives to maximize profits. The researchers also assess the influence of the performance of the owner's perception on the implementation of GCG.

The purpose of this study is to determine the differences in the implementation of bank governance and the application of risk management. Besides that, it also to determine the impacts of the implementation of GCG and the application of risk management to the performance of banks before and after the Financial Services Authority applied.

II. Methodology

The type of research is explanatory that describes the variables and the influence of one variable with other variables [10]. GCG data is obtained from the GCG implementation report sent by the bank and validated by Bank Indonesia. Bank performance data (ROA, ROE) and risk management data (CAR, NPL, LDR, BOPO) are also obtained from Bank Indonesia. The entire data analyzed was generated from secondary data from all commercial banks in Indonesia which combined data on GCG, risk management, and bank performance.

The study population is 43 public banks in Indonesia was listed on the Indonesia Stock Exchange in 2009-2016. The research sample is foreign banks, government and private sector which can be obtained from the period of 2009-2016. The total sample is 25 banks that have complete data for the period 2009-2012 (before OJK regulations apply) and data for the period 2013-2016 (after OJK regulations apply). The sample selection technique is purposive sampling.

Based on the analysis tool used is Structural Equation Modeling (SEM), the number of samples is the number of indicators multiplied by 5-10 because of the number of indicators. Since the number of indicator for this study is 11, hence the number of samples is between 55 to 110 or even more than 110. After considering that, the number of samples used for this study is 200 [11]. Multivariate analysis in this study using SEM path diagram function to show the pattern of relationships between variables studied through Partial Least Square (PLS).

III. Results

Data analysis technique using SEM used to describes the relationships between variables in the study. The goodness of fit models is measured using R-square dependent latent variables with the same interpretation by Q-Square Predictive Relevance regression. The interpretation is for structural models governing how well the observation value is generated by the model and also its parameter estimates.

The variable Bank Performance (R^2 = 0.102> 0.75) indicates that this variable is predicted strongly in the model. The variable degree value (R^2 = 0.836> 0.75) indicates that this variable is predicted strongly in the

model. Evaluation of the structural equation model as a whole using the GOF index obtained results showing that the model has a large GOF index value of 0.567 [12]. To see the influence between exogenous and endogenous variables on the model of firm value is shown in Table 1.

Table 1. Evaluation of R-square value according to research variables

Variable	R *Square*
GCG	-
Bank Performance	0.319332
Risk Management	-
Corporate Value	0.914540

Source: output SmartPLS 3.0, 2017

The inner model structural equation is obtained from the path coefficient and R-Square values of each latent variable. It was obtained that the GCG, risk management and bank performance variables on the company value were 91.5%. While the contribution of GCG and risk management variables to bank performance amounted to 31.9%. Based on table 2, it can be seen the results of measurements of path coefficients, the relationship between variables in the structural model.

Table 2. Results of Measurement of Path Coefficients, Relations between variables on Structural Model

Relationship between variables	Rho	t >1,96	H_o	Conclusion
GCG □ Corporate Value	0.51	16.65	Rejected	Positive influence
Risk Management□ Corporate Value	0.54	15.07	Rejected	Positive influence
Bank Performance□ Corporate value	-0.16	5.06	Rejected	Negative Influence
GCG □ Bank Performance	-0.54	6.23	Rejected	Negative influence
Risk Management □Bank Performance	0.87	6.38	Rejected	Positive influence

Source: Taken from SmartPLS 2.0 report, 2017

Based on table 2, it can be seen that all variables have a statistic value greater than 1.96%. The value of GCG variable on corporate value is 16.658. Then, risk management for company value is 15.077. In addition, bank performance against firm value is 5.066, GCG on bank performance value is 6.236 and risk management on bank performance is 6.383. Then Ho is rejected because the t-statistic value is far above the critical value (1.96) at α 5%.

The pretest-posttest was carried out to determine whether OJK regulations influence GCG, risk management, bank performance and /corporate value. Hence, the OJK regulations on national banking regulations can be used by banks as a guideline for financial services authorities.

Table 3. Analysis of changes in GCG, risk management, bank performance, and corporate values before and after the implementation of OJK regulations

Variable	T	df	*p-value*	Conclusion
GCG	-2.24	99	0.027	Significant
Risk management	7.65	99	0.000	Significant
Bank performance	-1.68	99	0.096	Not-significant
Corporate value	-0.70	99	0.483	Not Significant

Based on the result of the dependent t-test, there are differences in the average value of GCG, risk management, bank performance and corporate value before and after the OJK regulations implementation. If the p-value is less than 0.05, it shows that the implementation of the OJK regulation has a significant impact. While if the p-value is greater than 0.05, it means that no differences between before and after the implementation for particular variables. As shown in Table 3 above, there are significant differences between GCG (p-value = 0.027) and risk management (value p = 0.000) before and after the OJK regulations implementation. On the other hand, it does not give a significant impact on bank performance and corporate value. It can be seen based on the bank performance value (p-value = 0.096) and company value (p-value = 0.483). Hence, the

interpretation of this finding is that the current OJK regulations are effective enough to improve GCG and reduce company risk.

The regulation and supervision of banks are directed to optimize the functions of Indonesian banking as: (1) institutions of public trust is as an institution to collect and distribute funds. (2) encouraging the realization of a strong and efficient banking system to create financial system stability in order to help the national economic growth.

In order to achieve those objectives, the followings approach should be implemented: (1) policies that provide business flexibility (deregulation). (2) bank prudential banking policies and (3) bank supervision which encourages banks to consistently implement internal regulations made by themselves (self-regulation banking) in their operational activities while still referring to the principle of prudence.

IV. Discussion

Effect of GCG on Corporate Value

The result of this study shows simultaneously that GCG has a significant and negative result of financial performance. The results of this study are in line with integrated risk management and good corporate governance GCG implementation which are an obligation recently. [13] found that the implementation of GCG had a significant effect on financial performance.

Effect of Risk Management on Corporate Value

The results of risk management test show that risk management has a significant impact on corporate value. It can be seen in the t-statistic value which 15.08 since the value is greater than 1.96. Therefore, Ho is rejected, while Ha is accepted that means the path analysis coefficient is significant. The path coefficient value between risk management and company value is 0.544. It shows that if other variables are constant, the value of the company will increase by 0.544 if only the risk management value rises by one unit. Risk Management contributes significantly to corporate value. Risk Management is an effort to minimize risk to the company. Management can assist in reducing information asymmetry within the company.

According to [14] the GCG implementation that indicated with CGPI value does not prove to have an effect on the corporate value. This is contradicting with [15] findings that conclude that GCG implementation had an effect on the corporate value. On the other hand, based on the study that was conducted by [16], [17] and [18], GCG does not affect the corporate value.

Effect of Bank Performance on the Corporate Value

The t-statistic value is greater than 5.07 it shows that bank performance contributes significantly on the corporate value. Due to the value of bank performance is greater than 1.96 in t-statistic, therefore Ho is rejected and Ha is accepted which means that the path analysis coefficient is significant. The path coefficient value between the performance of the bank and the company value is -0.167. Meaning that if other variables are constant then the value of the company will decrease by -0.167 if the performance value of the bank rises by 1 unit. Thus, the performance of banks has not been able to increase corporate value. However, it contributes significantly to corporate value.

Effect of *GCG* on Bank Performance

The GCG test results contribute significantly to the performance of the bank obtained by the t-statistic value of 6.24. Because the value of the GCG variable has a t-statistic value greater than 1.96. So, the path analysis coefficient is significant. Hence, Ho is rejected and Ha is accepted. The path coefficient value between GCG and bank performance is -0.549. It shows that if other variables are constant. The bank's performance will decrease by -0.549 if the GCG value rises by 1 unit. This means that GCG has not been able to improve banking performance. However, GCG contributes significantly to bank performance. Implementation of GCG has a negative effect on company performance. The board of commissioners is not able to improve the performance. In fact, they responsible and authorized to provide direction and supervise the management in preparing the company's financial statements.

The board of commissioners requires competency support, job description and coordination with other board members to perform the duty. The duty is to provide the direction and supervise the board of directors in their duties and managing the company which has not yet affected the banking performance. In addition, other duties monitor and control professional management in order to reduce all forms of fraud. Besides that, it is also to ensure the company's interests are maintained and an independent commissioner is formed. The independent commissioner is a member of the board of commissioners who are not affiliated with management and other members of the board of commissioners and controlling shareholders. Independent commissioners have not been able to improve banking performance.

Effect of Risk Management on Bank Performance

The risk management test results contribute significantly to bank performance which can be seen through the value of t-statistic which is 6.38. Due to the value of risk management variable has a t-statistic value greater than 1.96, hence Ho is rejected and Ha is accepted. Meaning that the path analysis coefficient is significant. The path coefficient value between risk management and bank performance of 0.870. It shows that if other variables are constant, the bank's performance will increase by 0.870 if the risk management value rises by 1 unit. Therefore, risk management contributes significantly to the bank's performance.

According to [19] who found that ERM has a significant effect on firm value. The results of this study are different from the results of the study found by [20] that there is no influence between ERM and firm value. Risk management is carried out to improve the performance of organizations or companies through pension funds so that it can reduce risks that may occur. [21] stated that risk management encourages improvements in organizational performance, especially in the awareness of risk will affect the low-risk profile of the capital market.

Effect of the Financial Services Authority Formation

The goal of the financial services authority is all activities in the financial services sector: be organized regularly, fairly, transparently, and accountability. Besides that, the aims are to able to realize a financial system that grows sustainably and stable and able to protect the interests of consumers and society.

OJK banking supervision and Bank Indonesia compile regulations to create synergic rules. The steps of OJK and Bank Indonesia synergize of competency and personnel in equating perceptions that can produce a robust banking system order. OJK and Bank Indonesia and exchanging and merging information systems. Both institutions can access banking information available in each institution timely (basis) so that it can support the effectiveness of the implementation of tasks. OJK and Bank Indonesia (BI) in performing their respective duties by making reciprocal relations. BI under certain conditions will conduct special checks on banks after coordinating with OJK. On the contrary, OJK identifies the problem of a particular bank that is experiencing a deteriorating condition, the OJK will submit information to BI. In reciprocal collaboration, it is useful to anticipate the negative systemic impact of banking conditions. In the event of an investment management violation. OJK formed a task force to handle alleged illegal actions in the field of investment management (Investment Alert Task Force).

V. Conclusion

Based on the findings and discussion in this study, it can be concluded that the implementation of GCG in banking operation has a positive impact on the bank value. The management is able to use earnings management in preparing the financial statement process so that it can affect the level of profit. It is also expected to improve the corporate value in a specific time.

The implementation of risk management in banking operations will have a positive impact on bank corporate values. Risk management is an effort to minimize risks to the company. Management can help reducing information asymmetry within the company so that the implementation of risk management has a positive effect on banking value.

Moreover, risk management in banking operation has a positive impact on baking performance. One of the negative effects of the company's performance on the value of the company is caused by external factors of the company. For examples: economic conditions and relationships of other stakeholders outside the company. If the relationship between the manager and other parties goes accordingly, then the problems between the two parties will not occur.

GCG has a negative effect on company performance. The more concentrated company ownership in one person, the more powerful the control will be and tends to suppress agency conflict. The greater the proportion of management ownership in a company, the management will work harder to fulfill the interests of shareholders who are also themselves. In addition, other duty is to monitor and control professionally management so that it can reduce all forms of fraud.

Banking performance has a negative effect on corporate value. This is caused by external factors of the company, including economic conditions, relationships of other stakeholders outside the company. If the action between the manager and other parties goes accordingly, then the problem between the two parties will not occur. In reality, the harmonization of the interests of both parties does not cause problems.

The GCG implementation is increased towards the banking corporate value through the performance of the bank as an intervening variable towards the value of the company. GCG implementation has an impact on increasing the value of banking companies through company performance so that an increase in GCG will affect the indirect increase in the value of banking companies.

There is also an increase in risk management on the value of banking companies through the performance of banks as an intervening variable to the corporate value. The implementation of risk management

has an impact on increasing the value of the company. Hence, the increase in risk management will affect the indirect increase in the value of banking companies.

The role of the financial services authority has been able to increase the average value of the GCG mechanism and risk management. While the bank's performance and company value do not have a real difference when compared to before and after the establishment of the financial services authority. The government's role previously by Bank Indonesia has gone well, but the role of the government as a regulator played by the financial services authority has been able to improve banking performance effectively and efficiently.

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