International Seminar of Research Month
Science and Technology for People Empowerment
Volume 2018

NST PROCEEDINGS

OPEN ACCESS

Conference Paper

The Effect of Corporate Governance on Company Financial Performanceat Jakarta Islamic Index

I. Wikartika*, F. S. Akbar

Department of Management, Faculty of Economic and Business, Universitas Pembangunan Nasional "Veteran" Surabaya, East Java, Indonesia

Abstract

The economy in Indonesia is experiencing instability due to intense competition in the era of globalization and the international free market. Alongside this, the implementation of corporate governance in Indonesia is still not able to meet expectations. Thus, it becomes one of the causes of economic instability that has an impact on the company's financial performance. The Forum for Corporate Governance in Indonesia formulates corporate governance as a corporate governance system that explains the relationship of various participants in determining the direction and performance of the company. Corporate governance is one of the important non-financial components and needs to be considered in an effort to improve company performance. Besides, the development of the capital market in Indonesia could be an economic growth driver by increasing the investment activities. The strong role of the Islamic capital market in the formation of Indonesia's capital market capitalization indicates the Islamic capital market has a major role in driving Indonesia's economic growth. This study aims to analyze the influence of the board of commissioners, independent board of directors, the board of directors, and audit committee to the return on equity. The subject of the current research was a company registered in the Jakarta Islamic Index. Research samples were 30 companies registered in the Jakarta Islamic Index for the period June-November 2017. The data analysis techniques used was multiple linear regression. The results showed that the size of the board of commissioners, the board of directors, and the audit committee had no effect on return on equity while the independent board variable had an effect on return on equity.

Keywords: Comporate govermance, capital market, financial performance, return equity

INTRODUCTION

The economy in Indonesia has experienced instability from year to year. This situation is caused by intense competition in the era of globalization and the international free market. The implementation of corporate governance in Indonesia still cannot meet expectations so that it becomes one of the causes of economic instability which has an impact on the company's financial performance. Good Corporate Governance (GCG) has not provided a good governance solution for the company when compared to other Asian countries, Indonesia is still lagging behind in implementing corporate governance. GCG implementation requires a strong commitment to making it happen. The concept of corporate governance is proposed to achieve more transparent corporate management for all users of financial statements. If this concept is implemented properly, it is expected that economic growth will

* Corresponding author
Email address: irawikartika@upnjatim.ac.id

How to cite this article: Wikartika I & Akbar FS (2018) The Effect of Corporate Governance on Company Financial Performance at Jakarta Islamic Index. *International Seminar of Research Month Science and Technology for People Empowerment*. NST Proceedings. pages 412-420.doi: 10.11594/nstp.2019.0255.

continue to rise along with the transparency of the company's management that is getting better and later benefiting many parties (Nasution & Doddy, 2007). The issue of corporate governance is still an interesting discussion to be discussed in almost all parts of the world. This is because, issues related to corporate governance have been seen as important in addressing a company's financial problems (Rajput & Bharti, 2015).

The Forum for Corporate Governance in Indonesia (FCGI, 2001) formulates corporate governance as a corporate governance system that explains the relationship of various participants in determining the direction and performance of the company. The aim of corporate governance is to create added value for stakeholders. Effective corporate governance is expected to improve the company's financial performance. Corporate governance can be defined as a set of rules that determine the relationship between shareholders, managers, creditors, governments, employees, and other internal and external stakeholders in accordance with their rights and responsibilities. Corporate governance is one of the important non-financial components and needs to be considered in an effort to improve company performance.

Appraisal of company performance using financial measures is more often used because there are potential comparison standards, whether in the form of financial statements in the past or with financial statements of other similar companies. The company's financial performance can be measured by profitability ratios (Puspitasari & Ernawati, 2010). Return on Equity (ROE) is the most important ratio of corporate equity taking, shareholders definitely want a high rate of return on the capital they invest, and the ratio shown by ROE shows the rate of return they will get (Brigham & Houston, 2010). Basically, enforcement of good corporate governance is used to minimize conflicts between shareholders and company management (known as "agency theory"). In addition, good corporate governance is also used to create a business world that competes in a healthy manner and provides optimal contributions to stakeholders. Agency theory states that agency relations arise when one or more people (principals) employ another person (agent) to provide a service and then delegate decision-making authority to the agent (Jensen & Meckling, 1976). In agency theory, shareholders (principals) as parties who own shares fully request management (agents) to maximize returns for them. Agency problems arise when the objectives of the principal and the agent conflict. According to Jensen and Meckling (1976) corporate governance needs to act as monitoring in solving agency problems. Monitoring is a mechanism that is intentionally made by the principal to oversee the agent by forming a supervisory board (board of commissioners) and involving shareholders in overseeing the running of the company. Corporate governance systems provide effective protection for shareholders and creditors so that they are sure to get a return on their investment correctly. Corporate governance also helps create a conducive environment for the creation of efficient and sustainable growth in the corporate sector.

The Islamic capital market is part of the Indonesian capital market industry. In general, Islamic capital market activities are in line with the capital market in general. However, there are some special characteristics of the Islamic capital market, namely that the product and mechanism of transactions must not conflict with sharia principles in the capital market. The Islamic capital market is a capital market activity that does not conflict with sharia principles in the capital market. The role of the Islamic capital market is as a source of income for companies to develop their businesses through the issuance of sharia securities and as a means of investing in Islamic securities for investors. List of Sharia Securities (DES) is a collection of securities that do not conflict with sharia principles in the capital market, which are determined by Bapepam-LK. Sharia shares are securities in the form of shares that do not conflict with sharia principles in the capital market. All Islamic stocks contained in the Indonesian sharia capital market, whether or not listed on the IDX, are included in the DES issued by the Financial Services Authority (OJK) regularly every May and November. The Jakarta Islamic Index (JII) is a sharia stock index that was first launched in the Indonesian capital market on July 3, 2000. JII is a type of stock price index listed on the Indonesia stock exchange. JII uses 30 shares selected from stocks included in the Shariah or DES criteria issued by Bapepam-LK taking into account market capitalization and liquidity. There was a decrease in the value of return on equity in 2016 when compared to the previous year. In 2017 several companies in the Jakarta Islamic Index belong to the category of good corporate

governance. This phenomenon is the interest of researchers to conduct research on the effect of corporate governance on financial performance in the Jakarta Islamic Index.

Based on the background described above, the researcher is interested in proving the influence of corporate governance on financial performance. In this study using corporate governance as an independent variable is proxied by the board of commissioners, independent board of commissioners, the board of directors, and audit committee. The company's financial performance as the dependent variable is measured using Return on Equity (ROE). The research object used is a company registered in the Jakarta Islamic Index for the period from June to November 2017. Based on the description, the title of this research is "Analysis of the Effect of Corporate Governance on Corporate Financial Performance in the Jakarta Islamic Index".

METHODS

The type of research used is explanatory research with a quantitative approach that is used to determine and explain the effect of corporate governance on the company's financial performance. Explanatory research is research that is based on a theory or hypothesis that will be used to test a phenomenon. Secondary data is research data obtained. This research data is secondary data in the form of financial data and ratios (financial data and ratios) and annual reports of companies registered in the Jakarta Islamic Index obtained through the official IDX website, www.idx.co.id. The type of data used is pooled data. The method of data collection uses documentation techniques, namely collecting and studying the data needed. The research population used is all companies listed in the Jakarta Islamic Index for the period June to November 2017. The Jakarta Islamic Index (JII) is one of the indices on the Indonesia Stock Exchange (IDX). JII is a sharia stock index that has a high level of liquidity. The sample of this study is 30 companies listed in the Jakarta Islamic Index for the period of June to November 2017.

The dependent variable of this study is the company's financial performance which is proxied by using Return on Equity (ROE). ROE is the company's ability to generate profits from its capital (Putra & Nuzula, 2017). ROE = Net income after tax divided by total equity. The first independent variable is corporate governance which is proxied using the board of commissioners. The board of commissioners is the number of all board members in the company (Perdana, et al., 2016). Board of Commissioners = number of members of the board of commissioners. The second independent variable is corporate governance that is proxied by using an independent board of commissioners. Independent board of directors is a proportion of the number of independent commissioners who have no relationship with other members (Aprianingsih & Yushita, 2016). Independent board of commissioners = the number of independent commissioners divided by the number of members of the board of commissioners. The third independent variable is corporate governance that is proxied using a board of directors. The board of directors is the number of all members of the board of directors in the company (Wehdawati & Jikrillah, 2015). Board of directors = a number of board members. The fourth independent variable is corporate governance which is proxied by using an audit committee. The audit committee is the number of all audit committee members in the company (Mulyadi, 2016). Audit committee = a number of audit committee members.

The analytical model used is a multiple linear regression model. The multiple linear regression equation models in this study are as follows:

$$ROE = \alpha + \beta 1DK + \beta 2DKI + \beta 3DD + \beta 4KA + \varepsilon it$$

Information :

ROE = Return on Equity

DK = Board of Commissioners

DKI = Independent Board of Commissioners

DD = Board of Directors

KA = Audit Committee

Ɛit = Standard error.

RESULT AND DISCUSSION

Outlier test

Outlier detection can be shown if the value of maximum mahalonobis distance is greater than the probability and number of variables [= CHIINV (probability; number of independent variables)].

Table 1. Residuals Statistics[a]

Residuals Statistica[a]					
	Minimum	Maximum	Mean	Std. Deviation	N
Predicted Value	-3.0200	59.5961	16.9263	14.47350	30
Std. Predicted Value	-1.378	2.948	.000	1.000	30
Standard Error of Predicted Value	5.849	18.622	10.805	3.247	30
Adjusted Predicted Value	-6.0873	61.4341	16.0475	15.17042	30
Residual	-43.50065	86.49406	.00000	25.62494	30
Std. Residual	-1.576	3.134	.000	.928	30
Stud. Residual	-1.785	3.547	.014	1.085	30
Deleted Residual	-55.77412	125.70090	.87883	35.34078	30
Stud. Deleted Residual	-1.872	4.932	.101	1.394	30
Mahal. Distance	.336	12.236	3.867	3.019	30
Cook's Distance	.000	1.632	.090	.311	30
Centered Leverage Value	.012	.422	.133	.104	30

a. Dependent Variable: ROE

Table 1 presents maximum Mahalanobis distance value of 12.236 is smaller than 18.467 [CHIINV (0.001; 4)]. This value shows there are no outliers in the observation data, which means that the observation data has good quality so that further processing can be carried out.

Normality test

Normality of a regression model where the dependent and independent variables or both have a normal distribution or not. Normality detection using the Kolmogorov-Smirnov Test shows that all research variables have a normal distribution if the value of Asymp. Sig (significance) is smaller than 0.05.

Table 2. One-Sample Kolmogorov-Smirnov Test

		ROE	DK	DKI	DD	KA
N		30	30	30	30	30
Normal Parameters[a,b]	Mean	16.9263	5.8333	.3603	6.5000	3.3333
	Std. Deviation	29.42991	2.16689	.13830	1.81469	.80230
Most Extreme Differences	Absolute	.405	.136	.220	.175	.428
	Positive	.405	.136	.220	.175	.428
	Negative	-.284	-.131	-.180	-.104	-.306
Test Statistic		.405	.136	.220	.175	.428
Asymp. Sig. (2-tailed)		.000[c]	.164[c]	.001[c]	.019[c]	.000[c]

a. Test distribution is Normal.
b. Calculated from data.
c. Lilliefors Significance Correction.

The results of the analysis show that the variables ROE, DKI, DD, and KA have Asymp values. Sig (significance) which is smaller than 0.05 while the DK variable has an Asymp.Sig value greater than 0.05. Thus it can be concluded that the data mostly have met the assumptions of the normal distribution.

Multicollinearity test

Multicollinearity is the existence of an independent variable correlation in multiple regression. Multicollinear Detection:

a. The amount of VIF (Variance Inflation Factor) and Tolerance. If the VIF number exceeds 10, the variable indicates multicollinearity.
b. The Eigenvalue is close to 0.
c. Condition Index exceeds number 15

Table 3. Coefficients[a]

		Collinearity Statistics	
		Tolerance	VIF
1	DK	.810	1.235
	DKI	.865	1.156
	DD	.802	1.246
	KA	.864	1.158

a. Dependent Variable: ROE

The results of the analysis show that all independent variables have VIF values smaller than 10 and have tolerance values close to 1. Thus it can be concluded that there are no symptoms of multicollinearity on all independent variables.

Heteroscedasticity Test

Heteroscedasticity is a variant of residuals from one observation to another having different variants. If the same is called homoskedasticity. Heteroscedasticity testing in this study uses Spearman rank correlation between residuals and all independent variables.

Table 4. Nonparametric Correlations

			Unstandardized Residual
Spearman's rho	DK	Correlation Coefficient	-.242
		Sig. (2-tailed)	.198
		N	30
	DKI	Correlation Coefficient	-.531**
		Sig. (2-tailed)	.003
		N	30
	DD	Correlation Coefficient	-.050
		Sig. (2-tailed)	.795
		N	30
	KA	Correlation Coefficient	.146

		Sig. (2-tailed)	.441
		N	30
	Unstandardized Residual	Correlation Coefficient	1.000
		Sig. (2-tailed)	.
		N	30

The results of the analysis show that the Sig value for the correlation in the variables DK, DD, and KA is greater than 0.05 while in the DKI variable the value for correlation is smaller than 0.05. This means that the three variables do not have a significant correlation between the residuals and the independent variables while the DKI variables have a significant correlation between the residuals and the independent variables. Thus it can be concluded that most of the research variables do not occur heteroscedasticity but there is one variable that has heteroscedasticity.

Autocorrelation Test

Autocorrelation is a correlation between periodic error with period t-1 (previous). Autocorrelation Detection:

a. Durbin Watson Test
b. High coefficient of multiple determination (R square)
c. The correlation coefficient is simply high.
d. High calculated F value (significant)
e. But none (or very few) of significant independent variables.

Table 5. Model Summary [b]

Model	Durbin-Watson
1	2.312[a]

a. Predictors: (Constant), KA, DKI, DK, DD

b. Dependent variable: ROE

This study uses the Durbin Watson test. Based on the results of data processing, the Durbin Watson (dW) value of 2.312 is located between the 4-dU region and 4-dL, this means that it lies in the area of doubt. Thus it can be concluded that there is no autocorrelation.

Coefficient of determination

The coefficient of determination (R2) of 0.242 means that the dependent variable namely return on equity is influenced by independent variables namely board of commissioners, independent board of commissioners, the board of directors, and audit committee of 24.2% while the remaining 75.8% is influenced by other variables besides independent variable in the model.

Table 6. Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.492[a]	.242	.121	27.59890

Predictors: (Constant), KA, DKI, DK, DD

b. Dependent Variable: ROE

Suitability model (F Test)

Tabel 7. ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	6074.987	4	1518.747	1.994	.026[b]
	Residual	19042.488	25	761.700		
	Total	25117.476	29			

a. Dependent Variable: ROE

b. Predictors: (Constant), KA, DKI, DK, DD

The test results show a significance value (Sig) of 0.026 smaller than 0.05 which means significant, so it can be concluded that the use of the regression model in this study is appropriate.

Hypothesis testing

Table 8. Coefficients[a]

Unstandardized Coefficients	
B	**Std. Error**
32.532	29.734
2.579	2.628
102.464	39.849
.153	3.153
.454	6.873

a. Dependent Variable: ROE

The multiple regression equation is as follows:

ROE = 32,532 + 2,579 DK + 102,464 DKI + 0,153 DD + 0,454 KA + ei

Based on the multiple regression equation models above, it can be interpreted as follows:

a. The constant value of 32,532 indicates that if the other independent variables are constant, then the value of return on equity is 32,532%.
b. The regression coefficient for X1 of 2.579 which is positive indicates a unidirectional relationship between the board of commissioners and return on equity, which means that if the board of commissioners increases by 1%, the return on equity value will increase by 2.570% assuming the other variables are constant.
c. The regression coefficient for X2 of 102.464 which is positive indicates a unidirectional relationship between the independent board of commissioners and return on equity, which means that if the independent board of commissioners increases by 1% then the return on equity value will increase by 102.464% assuming the other variables are constant.
d. The regression coefficient for X3 of 0.153 which is positive indicates a unidirectional relationship between the board of directors and return on equity, which means that if the board of directors increases by 1%, the return on equity value will increase by 0.153% assuming the other variables are constant.
e. The regression coefficient for X4 of 0.454 which is positive indicates a unidirectional relationship between the audit committee and return on equity, which means that if the audit committee increases by 1%, the return on equity value will increase by 0.454% assuming the other variables are constant.

The influence of the Board of Commissioners on ROE

Based on the results of the analysis show that the board of commissioners variable has a significance value of 0.336 greater than 0.05, which means the size of the board of commissioners has no influence on return on equity at

the level of 5%. This is because the existence of the board of commissioners is only used to meet regulatory requirements and not to establish good corporate governance, causing the supervisory function that should be run by the board of commissioners to be ineffective. Determination of the number of optimal membership of the board of commissioners must also be adjusted to the needs and complexity of the company's activities. These results support the research of Perdana, et al. (2016) and Wehdawati & Jikrillah (2015) whose research results reveal that the size of the board of commissioners does not affect return on equity.

The influence of the Independent Board of Commissioners on ROE

Based on the results of the analysis show that the independent board of commissioners variable has a significance value of 0.016 smaller than 0.05, which means that the independent board of commissioners has an influence on return on equity. This is in accordance with the general guidelines for the implementation of corporate governance stating that the existence of independent commissioners must ensure that the oversight mechanism runs effectively. These results support the research of Perdana, et al. (2016), whose results reveal that the size of independent commissioners influences returns on equity.

The influence of the Board of Directors on ROE

Based on the results of the analysis show that the board of directors variable has a significance value of 0.862 smaller than 0.05, which means that the board of directors has no effect on return on equity. This is because determining the optimal number of members of the board of directors is very difficult and depends on the complexity of the company's activities. The role of shareholders still dominates so that the board of directors cannot optimally carry out their authority and responsibility properly. These results support the research of Wehdawati & Jikrillah (2015) which revealed that the size of the board of directors does not affect return on equity.

The influence of the Audit Committee on ROE

Based on the results of the analysis, the audit committee variable has a significance value of 0.648 greater than 0.05, which means that the audit committee has no influence on return on equity. This is because the existence of an audit committee is only used to meet regulatory requirements and not to establish good corporate governance so that the role of the audit committee cannot be maximally carried out in its authority and responsibility. These results support the research of Mulyadi (2016) and Putra & Nuzula (2017) whose results reveal that audit committees do not affect return on equity.

CONCLUSION

Based on the results of the analysis and discussion it can be concluded that:

1. The variable number of board of commissioners has no influence on return on equity.
2. The variable number of independent commissioners has an influence on return on equity.
3. The variable number of board of directors has no influence on return on equity.
4. The variable number of audit committees has no effect on return on equity.

ACKNOWLEDGEMENT

The authors also thank to the Universitas Pembangunan Nasional "Veteran" Surabaya, East Java, Indonesia and all related parties that support the implementation of this research so that can be completed properly.

REFERENCES

Brigham, E. F. & Houston, J. (2010). *Dasar-dasar Manajemen Keuangan.* Jakarta: Salemba Empat.

Jensen, M. C. & Meckling, W. H. (1976). Theory of The Firm : Manajerial Behaviour, Agency Cost, and Ownership Structure. *Journal of Financial and Economics, 3*(4), 305-360.

Mulyadi, R. (2016). Pengaruh Corporate Governance terhadap Kinerja Keuangan. *Jurnal Akuntansi 43*(1), pp. 1-15.

Nasution, M. & Doddy, S. (2007). *Pengaruh Corporate Governance terhadap Manajemen Laba di Industri Perbankan Indonesia.* Makasar, Simposiun Nasional Akuntansi, pp. 26-28.

Perdana, H. D., Putra, R. P., Murni, S. (2016). Corporate Governance dan Kinerja Keuangan Perusahaan (Studi pada Perusahaan Indonesia di Indeks LQ45 Tahun 2010-2014). *Jurnal Akuntansi, 4*(1), 1-10.

Puspitasari, F. & Ernawati, E., 2010. Pengaruh Mekanisme Corporate Governance terhadap Kinerja Keuangan Badan Usaha. *Jurnal Manajemen Teori dan Terapan 3*(2).

Putra, A. S. & Nuzula, N. F. (2017). Pengaruh Corporate Governance terhadap Profitabilitas. *Jurnal Administrasi Bisnis, 47*(1), 103-112.

Rajput, N. & Bharti. (2015). Shareholder Types, Corporate Governance and Firm Performance : An Anecdote from Indian Corporate Sector. *Asian Journal of Finance & Accounting*, 7(1).

Wehdawati, F. S. & Jikrillah, S. (2015). Pengaruh Mekanisme Good Corporate Governance dan Struktur Kepemilikan terhadap Kinerja Keuangan Perusahaan Manufaktur yang Terdaftar di BEI Tahun 2010-2012. *Jurnal Wawasan Manajemen 3*(3), 205-215.