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Determination of Company Profitability and Value of Banks in Indonesia Based on Risk Profile, Capital Structure, Corporate Governance and Asset Structure

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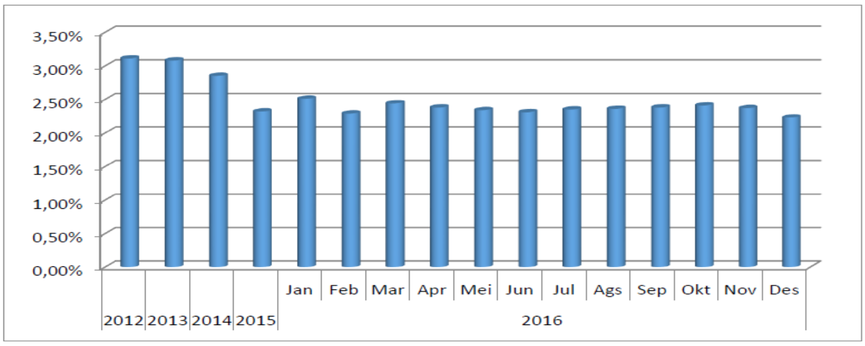
Abstract: This study aims to analyze and obtain empirical evidence about the effect of risk profile, capital structure, corporate governance and assets structure on profitability and the effect of profitability on corporate value. The object of the research is a banking company listed on the Indonesian stock exchange from 2011 to 2017. Data were analyzed using structure equation modeling with smart-pls software. Banks selected based on purposive sampling were 8 banks. The results proved that only the risk profile has a significant effect on profitability. While capital structure, corporate governance and assets structure did not have significant effect on profitability. The results also showed that profitability did not have a significant effect on corporate value. Therefore, profitability has not been proven to mediate the relationship between the exogenous variables studied on corporate value. In this study, the adjusted r-square of the corporate value was 52.6%. It means that the proportion of exogenous variables influencing the endogenous variables studied was 52.6%.

Keywords: The Role of Profitability, Bank Performance, Corporate Value.

INTRODUCTION

Banks are financial institutions that are very instrumental in the economic growth of a country. Where the role of banks is as an intermediary institution, which is an institution that channels funds from parties who have excess funds to individuals or entities that need funds to run a business. With the presence of banks, it is expected that the investment climate and business climate will be maintained. However, like other business institutions, bank performance can experience ups and downs. As in Indonesian banking statistics found stated by Otoritas Jasa Keuangan (banking authority) official website shows that the average performance of banks in Indonesia shown in the value of return on assets (ROA) from 2012 to 2015 shows an unvaforable trend, namely with a horizontal value and tendencies. It decreases in the range of 3% to 2.4% as shown in Figure 1.

Figure 1. Average Return on Bank Assets in Indonesia



Sources: Indonesian banking statistics (www.ojk.id)

Decline in the average performance of banks in Indonesia is something that should be aware and investigated. Therefore, the factors that influence the bank's profitability performance are interesting things to study. Another thing that is no less important is to generate public trust in bank performance by looking at the value of the company. With a reflection of the corporate value is expected to represent the performance of banks in the financial sector. Where the corporate value is strongly influenced by profitability. Based on the previous study, profitability showed a significant proportion in influencing corporate value (Ayu and Suarjaya 2017). Based on a literature review of previous research, there are several factors that can affect the bank's profitability performance. These include the bank's risk profile, capital structure, corporate governance, and bank asset structure (Manurung, Suhadak, and Nuzula 2014), (Nandaria and Kusuma 2014),(Saleh, Priyawan, and Ratnawati 2015),(Kristianti and Yovin 2016),(Nassar 2016). Therefore, this research is intended to conduct empirical analysis and verification on the influence of risk profile, capital structure, corporate governance, and assets structure on bank profitability. Then, this study also aimed to get empirical evidence about the role of profitability in shaping corporate value.

MATERIAL AND METHOD

The Effect of Risk Profiles on Bank Profitability

The risk profile for banks in Indonesia is regulated in Bank Indonesia regulations. The risk profile reflects the bank's health performance. Increased risk owned by banks results in higher costs incurred by banks. Therefore, the bank's risk profile has an impact on profitability and of course on bank profitability. As explain in the previous studies, many research results have concluded that the factors that influence profitability of banks is risk profile (Kristianti and Yovin 2016), (Eng 2013). Based on these explanations the following hypothesis is formulated:

H_1: The risk profile has significant influence on bank profitability.

The Effect of Capital Structure on Bank Profitability

Bank is a form of business that requires high funding in carrying out its business. Ownership of company assets can be get from two main sources, namely from debt to third parties or funds from shareholders. Generally, the proportion of funds from third parties causes companies to be burdened with high interest. The greater the proportion of structure capital causes the greater the proportion of debt and the greater the interest expense that must be borne by the company. The greater interest expense that must be borne by the company causes a reduction in the proportion of profits derived by the company so that the impact on the decline in the value of the company's profitability. Therefore, capital structure can affect company profitability(Manurung et al. 2014), (Husaini 2013). Based on this explanation, the following hypothesis is formulated:

H_2: The capital structure has significant influence on bank profitability.

The Effect of Corporate Governance on Bank Profitability

Corporate Governance is a concept based on a regulatory framework for improving company performance through supervision or monitoring of management performance and ensuring management accountability to stakeholders(Tjondro, David. Wilopo 2011). So, with a good regulatory framework, supervision and assistance from stakeholders, it is expected that the company's profitability performance will also increase, and vice versa. In line with previous research that stated Corporate Governance affects the profitability of companies(Ukhriyawati, Ratnawati, and Riyadi 2017), (Nandaria and Kusuma 2014). Based on these explanations the following hypothesis is formulated:

H_3: The corporate governance has significant influence on bank profitability.

The Effect of Assets Structure on Bank Profitability

Assets are resources controlled by the company that are used for company operations and it is hoped that the benefits will be earned by the company in the future. Bank is a service industry that requires good asset management in carrying out its operations. Where these assets are used in bank operations to get income. So, with a good management of bank assets is expected to increase bank profitability. As with previous research states that the assets structure affect profitability(Saleh et al. 2015), (Mwaniki and Omagwa 2017). From the explanation above, the hypothesis is formulated as follows:

H_4: The assets structure has significant influence on bank profitability.

The Effect of Profitability on Corporate Value

The company's main goal is to generate profits, while profitability is a picture of the company's performance in generating profits. The high value of bank profitability illustrates the bank's good performance in generating profits. With high profit or profitability, it is expected to increase the value of the company. In line with previous studies in which company profitability has an influence on firm value(Wijaya and Sedana 2015). Based on this explanation, the following hypothesis is formulated:

H_5: The profitability has significant influence on corporate value.

The Role of Bank Profitability as Mediation Variable

As explained previously that the risk profile, capital structure, corporate governance and assets structure have an influence on bank profitability(Subandi and Ghozali 2014), (Manurung et al. 2014), (Saleh et al. 2015). Then there is also the effect of profitability on firm value(Wijaya and Sedana 2015). From this explanation, the assumption arises that when the risk profile, capital structure, corporate governance and asset structure change will cause changes in profitability. Then because the changes in profitability arise, the value of the company will also change. Based on this explanation, we can draw the conclusion that profitability is a variable that mediates the effect of risk profile, capital structure, corporate governance and asset structure on firm value. Based on the explanation above, the following hypothesis is formed:

H_6: Profitability mediates the effect of risk profile, capital structure, corporate governance and assets structure on the bank's corporate value.

DATA ANALYSIS

The approach used in this study is a quantitative approach by examining specific populations and samples aimed at testing the hypotheses that have been set(Sugiyono 2012). The analysis model used is structural equation modeling (SEM) using Smart PLS software. The variables of this study consisted of exogenous, moderating and endogenous variables.

Variables Measurement

There are two main variables used in this research, namely exogenous and endogenous variables. In addition, researchers include intervening variable in the research model. Here is the definition of each variable:

Exogenous Variables

Exogenous variables in this study are the risk profile, capital structure, corporate governance, and asset structure. The following indicators and measurements of each operational variable:

Table 1. Operational Definition of Exogenous Variables

No	Variable	Indicator	Measurement
1	Risk Profile	Loan to Deposit Ratio (LDR)	$= \frac{Total\ Credit}{Total\ Third\ Party\ Funds} x100\%$
		Non-Performing Loan (NPL)	$= \frac{Total\ Non\ Performing\ Loan}{Total\ Credit} x100\%$
		Net Interest Margin (NIM)	$= \frac{Net\ Interest\ Income}{Average\ Earning\ Assets} x100\%$
2	Capital Structure	Debt Ratio (DR)	$= \frac{Total\ Debt}{Total\ Assets} x100\%$
		Debt to Equity Ratio (DER)	$= \frac{Total\ Debt}{Total\ Shareholder\ Equity} x100\%$
3	Corporate Governance	Proportion of Independent Commissioners (Kind)	$= \frac{Number\ of\ Independent\ Commissioners}{Total\ Members\ of\ The\ Board\ of\ Commissioners} x100\%$
		Number of Audit Committees (AC)	$= The\ Number\ of\ Members\ on\ The\ Audit\ Committee$
		Percentage of Managerial Ownership (MO)	$= \frac{Number\ of\ Management\ Shares}{Number\ of\ Shares\ Outstanding} x100\%$
4	Asset Structure	current assets to total assets (CATA)	$= \frac{Total\ Current\ Assets}{Total\ Assets} x100\%$
		fixed assets to total assets (FATA)	$= \frac{Total\ Fixed\ Assets}{Total\ Assets} x100\%$

Source: Taken from various studies

Endogenous and Moderating Variables

This study uses profitability as a variable that is influenced by the four exogenous variables above. This research also places profitability as a moderating variable. While the endogenous variable of profitability is corporate value. The following table measures endogenous and exogenous variables:

Table 2. Operational Definitions of Endogenous and Moderating Variables

No.	Variable	Indicator	Measurement
1	Profitability	Return on Assets (ROA)	$= \frac{Income\ Before\ Tax}{Average\ of\ Total\ Asset} x100\%$
		Return on Equity (ROE)	$= \frac{Income\ After\ Tax}{Total\ Assets} x100\%$
2	Corporate Value	Price Earnings Ratio (PER)	$= \frac{Stock\ Market\ Prices}{Earnings\ per\ Share} x100\%$
		Price Book Value (PBV)	$= \frac{Market\ Price\ per\ Share}{Book\ Value\ per\ Share} x100\%$

Source: Taken from previous studies

Population and Sample

Population is a research object that has certain qualities and characteristics determined by researchers to be studied and then drawn conclusions (Sugiyono 2012). The population in this study is the most recent data released by the Indonesia Stock Exchange (IDX). Samples are selected using a purposive sampling technique that is the selection of samples based on a certain criterion(Jogianto 2010). The criteria set are as follows:

1. All banks listed on the Indonesia Stock Exchange that continuously report their financial statements during the study period are 2011 to 2017.
2. Company that never had a loss during the study period.
3. Companies that attach required data such as data from independent commissioners, audit committees, managerial ownership and other data needed in calculating the variables studied.

Based on the results of the sample selection, only 8 companies fulfilled the sample selection criteria for a period of 7 years, namely from 2011 to 2017.

RESULT AND DISCUSSION

In this study, data analysis begins with a statistical analysis of the description then proceed with inferential statistical analysis. Descriptive statistics are intended to get an overview of the data such as minimum and maximum scores, and the mean of the observed data. While inferential statistics are intended to test hypotheses or relationships between variables. The inferential statistical testing of the data is done using structural equation models (SEM) techniques using Smart sPLS Software. The following is a description of the data examined:

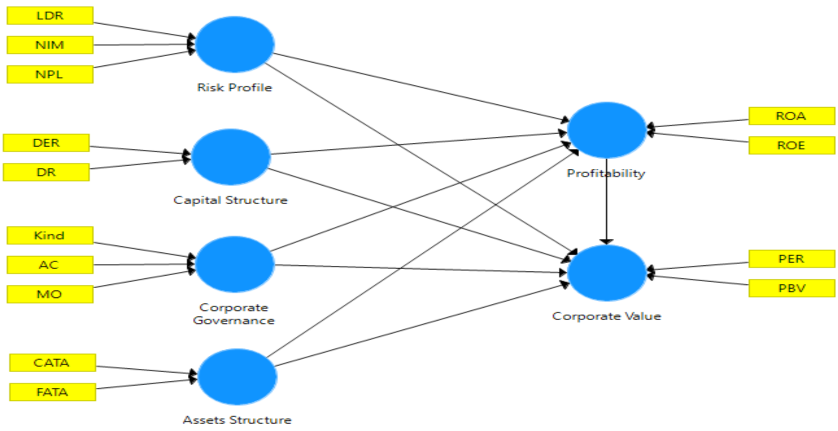
Table 3. Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
LDR	56	44.23	876.77	99.14	108.53
NPL	56	0.48	28.69	5.69	5.87
NIM	56	1.28	12.17	5.63	2.92
DR	56	76.17	123.01	86.05	6.81
DER	56	320.89	1,562.02	699.74	269.54
Kind	56	50	80	61.27	9.53
CA	56	3.0	6.0	4.14	1.13
MO	56	3.0	7.0	4.08	1.16
CATA	56	91.5	99.3	97.21	1.47
FATA	56	.7	8.5	2.78	1.47
ROA	56	.3	4.7	2.12	1.31
ROE	56	1.5	40.2	12.59	8.35
PER	56	1.8	29.6	9.06	5.81
PBV	56	6.4	35,040.0	4,977.49	8,810.33

Source: Data processed by researchers

Hypothesis analysis begins with the formation of a research model through a path diagram as shown in Figure 2. When forming a path diagram, consideration is needed whether the construct model used is formative or reflective. In this study the construct indicator model used is Formative. This was concluded based on testing the loading factor of each latent variable indicator. Almost all indicators on the latent variables studied have values less than 0.7. This indicates that each indicator is not a single unit that can be measured into latent constructs or changes to the construct do not cause changes to the indicators. Based on these characteristics, the indicator model used is formulated as a formative model (Ghozali, Imam. Latan 2015).

Figure 2. Path Model



Source: Data processed by researchers

Because the model indicators used is the formative model, there is no need to test the construct validity and reliability (Ghozali, Imam. Latan 2015). Therefore, testing continues directly to the inner model test. Variables are considered to have a significant effect on other variables when they have a p-value of less than 0.05 or 5%. The results of testing the inner model are shown in table 4 below:

Table 4. Result of Inner Model

	T Statistic	P Values	Conclusion
Risk Profile -> Profitability	2,836	0,005	Accepted
Capital structure -> Profitability	0,494	0,621	Not Accepted
Corporate Governance -> Profitability	0,774	0,457	Not Accepted
Assets Structure -> Profitability	0,995	0,320	Not Accepted
Profitability -> Corporate Values	0,942	0,347	Not Accepted

Source: Data processed by researchers

Based on the results of the inner model testing, it appears that only the risk profile has a significant effect on profitability. While, this study cannot prove that there is a significant relationship among the other four relationships, namely capital structure on profitability, corporate governance on profitability, assets structure on profitability and profitability on corporate value. From the result, we can also conclude that profitability is not proven to mediate the relationship between risk profile, capital structure, corporate governance and asset structure on corporate value.

As formulated in the research hypothesis, risk profile significantly influences bank profitability. This proves that the indicators contained in the risk profile constructed in the research hypothesis are suitable for use as a measurement of the soundness of a bank as formulated by the regulator, namely Bank Indonesia. As previous research also found that the risk profile has a significant effect on bank profitability(Kristianti and Yovin 2016).

In this study, capital structure has not been proven to influence bank profitability. This can occur when the proportion of interest expense held by the bank does not fully affect the profit earned by the company. Table 3 show that average the NIM shows a value of 5.63%, this means that the proportion of income is quite high, so that the interest expense generated from the debt proportion does not significantly affect the profitability of the company. As where previous research which states that capital structure with long-term measurement does not significantly affect profitability(Tailab 2014).

In this study, corporate governance was not proven to have a significant effect on profitability. Corporate governance is symbolized by the supervision of independent commissioners, the audit committee and the role of key management. It proves that independent commissioners, audit committees and key management cannot significantly increase bank profitability. In line with previous research which obtained empirical evidence that corporate governance mechanisms do not have a significant effect on profitability(Permatasari and Novitasary 2014).

This research also cannot prove that there is a significant influence between asset structure on profitability. It proved that there is no a significant role of asset structure in influencing profitability. This can be caused by other factors that are more dominant in influencing profits other than the structure of bank assets. As previous research which states that there is no significant effect of asset structure on profitability(Ani 2014).

Furthermore, the study cannot prove that profitability have a significant effect on corporate value. It can occur because corporate value can be influenced by several factors besides profitability. Sometimes investors can act irrational so that the investment decisions they make don't consider the company's performance. As stated in previous research that proven profitability does not have a significant effect on corporate value(Putri and Rachmawati 2017).

In this study the adjusted r-square of the corporate value is 0.526 or 52.6%. This means that the proportion of exogenous variables in influencing the endogenous variables studied was 52.6% and there were other variables outside the studied variables that affected corporate value by 47.4%. The adjusted r-square of profitability is 0.614 or 61.4%. This means that the proportion of exogenous variables in influencing the endogenous variables studied was 61.4% and there were other variables outside the variables studied that affected the corporate value of 38.6%.

CONCLUSION

Based on the results, we found that only the risk profile has a significant effect on profitability. While capital structure, corporate governance and asset structure have a significant effect on profitability. These results prove that the indicators in the risk profile studied are worthy of consideration by bank management as a supporting factor for profitability. Because, if the risk profile increases it will reduce the level of profitability. The value of DR and DER in this study is relatively high, it should be noted by bank management. This is because an increase in the proportion of corporate structure will increase the interest expense on loans and will erode corporate profits. So, although in this study the corporate structure does not have a significant effect on profitability, bank management must continue to stabilize the value of capital structure so that there is no decline in profit.

The role of corporate governance that not implement maximally also needs to become a concern of bank management. This requires bank management to maximize the role of corporate governance to increase profitability and corporate value. Then, the asset structure also needs management attention. As a goal the company has assets to be maximized to get profits. Therefore, management needs to manage assets more optimally to improve the company's profitability performance. Profitability is not proven to mediate the relationship between the variables studied. It is occur because profitability has no significant influence on corporate value.

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