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The Influence of Good Corporate Governance on Profitability in Manufacturing Companies Listed in the Indonesia Stock Exchange in 2020

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Abstract

This research on profitability aims to examine the effect of good corporate governance on profitability. The population in this research are manufacturing companies listed on the Indonesia Stock Exchange in 2020. The sample in this research was selected through purposive sampling, so that a sample of 163 companies was obtained. The statistical test tool uses multiple regression analysis. Profitability in this research was measured using Return on Assets, while good corporate governance was measured using the number of independent board of commissioners. The results show that the independent board of commissioners has a significant positive effect on profitability.

Keywords
good corporate governance; independent board of commissioners; profitability; Return on Asset

I. Introduction

Good corporate governance are the principles that underlie a process and mechanism for managing a company based on laws and regulations and corporate ethics (Peraturan Menteri Negara Badan Usaha Milik Negara No. PER-01/MBU/2011). According to Pelamoni (2013, in Abdillah, 2015), the board of commissioners is an internal mechanism of corporate governance that performs the oversight function. Research which was conducted by Putra (2015) shows that the more the number of independent commissioners in a company, the more stringent the supervision of the management and the board of directors will be so that the management and the board of directors always follow the wishes of the shareholders. The more the board of commissioners, the more input to the board of directors, so that the options obtained by the board of directors are more and more. Therefore, the addition of a board of commissioners will increase the company's performance.

Putri and Muid (2017) explained that with the existence of an independent board of commissioners, it is hoped that the supervisory function of the board of directors and company management will be more optimal and the assessment of management performance will be more objective. It is hoped that with this supervision, the company's management will continue to improve its performance, which will also have an impact on increasing the company's performance. According to Sarafina and Saifi (2017), financial performance is the main benchmark for measuring whether or not a company's performance is good. Whether or not the company's performance can be seen from the company's financial statements.

Research conducted by Rini and Ghozali (2012), Putra (2015), Sarafina and Saifi (2017) and Puspa et al (2021) shows that independent commissioners have a significant positive effect on profitability, while research conducted by Putri and Muid (2017) indicates that the independent board of commissioners has a significant negative effect on profitability. Meanwhile, research conducted by Candradewi and Sedana (2016) shows that the independent board of commissioners has an insignificant positive effect on profitability.

II. Review of Literature

2.1 Agency Theory

Agency theory is the basis used to explain corporate governance (Putri and Muid, 2017). Jensen and Meckling (1976, in Puspa et al, 2021) describe an agency relationship that occurs in one or more people (principals) to provide a service, then delegate decision-making authority to the agent. Andriyani and Mudjiyanti (2017) state that within the framework of agency theory there are three kinds of agency relationships, namely agency relationships between managers and owners, agency relationships between managers and creditors, and agency relationships between managers and the government. Based on the three agency relationships, managers have a tendency to convey or report the information they have in a certain way based on who they relate to, whether with owners, creditors or the government.

Corporate governance is a concept based on agency theory, which is expected to function as a tool to reduce information asymmetry between principals and agents (Putri and Muid, 2017). This information asymmetry can be reduced by implementing Good Corporate Governance. With the existence of an independent board of commissioners and ownership of outside parties in a company, it is expected to be able to carry out more independent supervision and control of management performance so that management is more transparent in conveying financial and non-financial information to shareholders. This transparency minimizes the information gap received by shareholders and managers (Abdillah, 2018).

2.2 Good Corporate Governance

Good Corporate Governance are the principles that underlie a process and mechanism for managing a company based on laws and regulations and corporate ethics (Peraturan Menteri Negara Badan Usaha Milik Negara No. PER-01/MBU/2011). GCG principles, namely transparency, accountability, responsibility, independence and fairness and equality are needed to achieve business sustainability (sustainability) of the company by paying attention to stakeholders (KNKG, 2006).

Every company must ensure that the principles of GCG are applied to every aspect of the business and at all levels of the company. The supervisory function to ensure that GCG has been carried out in a company is carried out by an independent board of commissioners (Pelamonia, 2013 in Abdillah, 2015). Meanwhile, the more ownership from outside parties, the higher the demand for the implementation of GCG within a company so that management performance can be achieved. With the implementation of GCG in a management, it is expected to reduce information asymmetry between management and shareholders, especially outside shareholders. With the implementation of GCG in a company, it is expected to reduce information asymmetry between shareholders and management (Puspa et al, 2021).

According to OJK (2014) in the Indonesian Corporate Governance Roadmap, to measure the progress of the Indonesian capital market in implementing GCG and identify areas that need to be improved by taking into account the exemplary practices that apply at the international level, several initiatives to assess these practices have been carried out by several institutions international, namely:

a. Reports on the Observance of Standards and Codes (ROSC)

The World Bank in collaboration with the International Monetary Fund (IMF) conducted research on the principles of corporate governance compiled by the Organization for Economic Co-operation and Development (OECD). The results of the assessment are reported in the form of ROSC. The ROSC assessment of corporate governance is carried out by assessing the legal and regulatory framework, business practices, and compliance of public companies, and their enforcement capacity with the governance principles issued by the OECD.

b. Credit Lyonnais Securities Asia (CLSA)

Brokerage associations and investment groups together with The Asian Corporate Governance Association (ACGA) assess corporate governance in several Asia-Pacific countries by looking at the rules and practices of Corporate Governance, law enforcement, the political and regulatory environment, the application of accounting and auditing standards, and corporate governance culture.

c. Asean Corporate Governance Scorecards (ACGS)

ACGS was introduced by the Asean Capital Market Forum (ACMF) as a tool to rank public and public corporate governance performance in ASEAN. The ACGS assessment is based on publicly accessible documentation and aims to create a collection of public companies in the ASEAN region with good governance and which can be promoted to foreign investors.

2.3 Profitability

Profitability is the company's ability to make a profit in relation to sales, total assets and own capital. Profitability ratios are very important to know by users of financial statements because they inform how much the company's ability to generate profits, the greater the profit ratio shows the better management in managing the company, (Sartono in Angelia, N et al. 2020).

Profitability is the company's ability to generate profits within a certain period and is an important aspect that can be used as a reference by investors or owners to assess management performance in managing a company (Putri and Azizah, 2019). According to Darsono and Ashari (2004), profitability ratios include:

a. Gross Profit Margin (GPM)
   GPM is found by net sales minus cost of goods sold divided by net sales. This ratio is useful for knowing the company's gross profit from each item sold.
b. Net Proft Margin (NPM)
   NPM is found by dividing net income by net sales. This ratio describes the amount of net profit earned by the company on every sale made.
c. Return on Asset (ROA)
   ROA is found by dividing net income by the average total assets. This ratio describes the company's ability to generate profits from every one rupiah of assets used.
d. Return on Equity (ROE)

ROE dicari dengan laba bersih dibagi rata-rata ekuitas. Rasio ini berguna untuk mengetahui besarnya kembalian yang diberikan oleh perusahaan untuk setiap rupiah modal dari pemilik.

e. Earning Per Share (EPS)
The analytical tool used to see profits on a share basis is earnings per share which is sought by net income divided by shares outstanding. This ratio describes the amount of return on capital for each one share.

f. Payout Ratio
Payment ratio describes the percentage of cash dividends received by shareholders to net income earned by the company. Payment ratio is sought by dividing cash dividends by the company's net profit.

g. Retention Ratio
Retention ratio is a ratio that describes the percentage of net profit that is used to increase the company's capital. This ratio is sought by retained earnings divided by net income.

h. Productivity Ratio
Productivity ratio is found by net sales divided by average total assets. This ratio serves to describe the company's operational ability to sell using its assets.

Agency theory explains that the separation between ownership and control in a company will cause problems because of the difference in interests between shareholders as principal and management as agent (Jensen and Meckling, 1976). According to Abdillah (2018), managers have a tendency to behave opportunistically where managers take actions that are more profitable for themselves than for the interests of shareholders. This can happen because shareholders do not have the direct capability to monitor and control the activities carried out by managers. Corporate Governance is a system consisting of rules, measurements and factors that control a company. Good Corporate Governance can be a system that is able to harmonize the relationship between management and shareholders, namely through the oversight function, managerial function, and monitoring function in order to ensure the accountability of management performance to shareholders in carrying out the company's operational system.

The higher the implementation of Good Corporate Governance, which is marked by the larger the size of the independent board of commissioners, will have an impact on the tighter supervision of the company's financial performance in the hope that the financial performance will be better and more effective. The more effective financial performance is indicated by the increase in profitability.

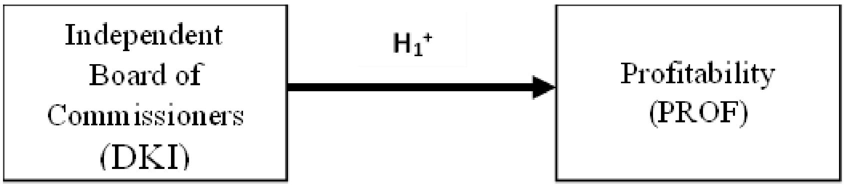

Figure 1. *Research Framework*

III. Research Method

This study uses a population of manufacturing companies that publish the 2020 financial statements of companies listed on the Indonesia Stock Exchange. The sampling in this study used purposive sampling, namely the sampling method based on certain criteria (Chandrarin, 2017). The criteria used in the sample research are:

a. The company is included in a group of manufacturing companies that publish financial reports every year and are listed on the Indonesia Stock Exchange (IDX) during 2020. The year 2020 was chosen because it describes relatively new conditions in Indonesia. By using a relatively new sample, it is hoped that the research results will be more relevant to understanding the actual conditions in Indonesia.
b. The financial statements have data related to research variables during the 2021 observation year.

Thus, based on the criteria used in this study, a sample of 163 manufacturing companies listed on the Indonesia Stock Exchange in 2020. The type of data based on the data sources used in this study is secondary data. Chandrarin (2017) states that secondary data is data that comes from parties or institutions that have used or published it so that testing the validity and reliability of secondary data is not necessary. This study uses secondary data in the form of financial reports on the Indonesia Stock Exchange because generally companies that go public have an obligation to report annual reports to parties outside the company, so that data can be obtained by researchers. The method used to collect data in this study is the documentation method. According to Sugiono (2015) documentation is a method used to obtain data and information in the form of books, archives, documents, writings, numbers and images in the form of reports and information that can support research. In this study, data were obtained by downloading financial statements and other related information from the official website of the Indonesia Stock Exchange and the company's official website. To determine the effect of independent commissioners on profitability, multiple regression analysis method was used with the following regression equation:

$$PROF = \alpha + \beta.DKI + e$$

Which is:
PROF = Profitability
DKI = Independent Board of Commissioners
α = model intercept
β = model regression coefficient
e = residual error

Variables and Operational Definitions

Chandrarin (2017) defines a variable as something or anything that has value and can be measured, both tangible and intangible. Variables must be clearly defined both conceptually and operationally, in other words, variables must be measurable. The variables used in this study are:

1. Independent Variable

   The independent variable is a variable that is thought to have an effect on the dependent variable (Chandrarin, 2017). The dependent variable in this study is the Independent Board of Commissioners as measured by the number of independent commissioners in the company.

According to Putri and Muid (2017), an independent board of commissioners is a board of commissioners whose members do not come from the board of directors or shareholders. OJK Regulation No. 33/POJK.04/2014 states that if the board of commissioners consists of two people, then one of them is an independent board of commissioners. If the board of commissioners consists of more than two people, then the number of independent commissioners must be at least 30% of the total members of the board of commissioners. Andriyani and Mudjiyanti (2017) state that the purpose of supervisory activities by an independent board of commissioners is to give a signal to the market about the reputation of effective supervisory activities within the company.

2. Dependent Variable

The dependent variable is the main variable that becomes the attraction or focus of research (Chandrarin, 2017). The dependent variable in this study is profitability as measured by using Return on Assets (ROA). ROA can be measured by comparing net income after tax divided by total assets (Darsono and Ashari, 2004).

According to Agustina and Soelistya (2018), profitability is the company's ability to earn profits from the business activities carried out. In other words, profitability is a measure of the level of profit generated by the company. The indicator used to measure profitability in this study is Return on Assets (ROA). ROA is used to assess whether the company is efficient in utilizing its assets in the company's operational activities. According to Darsono and Ashari (2004), ROA provides a better measure of company profitability because it shows the effectiveness of management in using assets to earn income. Lestari and Chariri (2007) stated that ROA has a more independent level in measuring profitability than ROE.

IV. Results and Discussion

In the current economic development, manufacturing companies are required to be able to compete in the industrial world. Manufacturing companies need to invest to increase the company's business capital. To invest, various kinds of information about the issuer are needed, both company performance information in the form of financial statements or other relevant information. The economic development of a country can be measured in many ways, one of which is by knowing the level of world capital market development. The capital market is a place for investors to conduct investment activities (Angelia and Toni, 2020).

Based on table 1 below, it can be explained that the independent board of commissioners (DKI) variable has a significance value of 0.000 (Sig. <0.05) and a positive regression coefficient of 0.075. This means that the independent board of commissioners (DKI) variable has a significant positive effect on profitability (PROF). Thus the research hypothesis is accepted.

This means that the more independent commissioners who oversee the financial performance of manufacturing companies listed on the Indonesia Stock Exchange (IDX) in 2020, the profitability will increase.

Table 1. t test results

Coefficients[a]

Model		Unstandardized Coefficients B	Unstandardized Coefficients Std. Error	Standardized Coefficients Beta	t	Sig.	Collinearity Statistics Tolerance	Collinearity Statistics VIF
1	(Constant)	-.099	.017		-5.761	.000		
	DKI	.075	.008	.575	8.917	.000	1.000	1.00

a. Dependent Variable: PROF

Source: Processed secondary data, 2021

Table 2. Coefficient of Determination

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.575[a]	.331	.326	.1006484	2.466

a. Predictors: (Constant), DKI

b. Dependent Variable: PROF

Source: Processed secondary data, 2021

The coefficient of determination essentially measures how far the model's ability to explain variations in the dependent variable is. The value of the coefficient of determination between zero or one. A small value of R^2 means that the ability of the independent variables in explaining the variation of the dependent variable is very limited. In table 2 it can be seen that the adjusted R^2 value is 0.326, this means that 32.6% of the variation in profitability (PROF) can be explained from the independent variable of the independent board of commissioners (DKI). While the rest (100%-32.6%=67.4%) was explained by other reasons outside the model.

KNKG (2006) states that the function of the independent board of commissioners is to carry out the functions of supervision, evaluation and dismissal of top managers. Therefore, the role of the independent board of commissioners in the company must be objective and not bound by any interests and parties. An independent board of commissioners is needed to oversee and control all opportunistic actions from management. The greater the number of independent commissioners, the more effective the role of independent commissioners in supervising management will be so that management will always act in the interests of shareholders. Companies that have a higher number of independent commissioners tend to have stricter and more objective supervision of the company's performance. This stricter and objective supervision encourages management to optimize company assets to improve company performance.

Puspa et al (2021) explained that in ensuring the creation of good GCG, independent commissioners are required to have good credibility, professionalism, and integrity. Independent commissioners will proactively encourage management to run the company in accordance with the wishes of shareholders and applicable regulations. Management will always be encouraged by the shareholders through the independent board of commissioners to always optimize the company's assets in increasing the company's performance. Research conducted by Putra (2015) found that increasing independent commissioners can improve company performance. Increasing the company's performance will increase the company's ROA.

The results of this study are in accordance with the results of research conducted by Rini and Ghozali (2012), Putra (2015), Sarafina and Saifi (2017) and Puspa et al (2021). However, it is not in accordance with the results of research conducted by Putri and Muid (2017) and Candradewi and Sedana (2016)

V. Conclusion

This study aims to examine the effect of independent commissioners on profitability. From the results of this study it can be concluded that the independent board of commissioners has a significant positive effect on profitability. Therefore, it can be interpreted that the greater the number of independent commissioners who oversee the financial performance of manufacturing companies listed on the Indonesia Stock Exchange (IDX) in 2020, the profitability will increase. The value of adj R2 on profitability is 0.326 so that the independent board of commissioners can explain the remaining 32.6% can be explained by other variables. Therefore, in further research, other variables can be added, such as external ownership structure, managerial ownership, institutional ownership, audit committee and company size.

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