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The Determinants of Financial Performance of State-Owned Banks in Indonesia

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Abstract---*Purpose: This study is to investigate the determinants of financial performance of state-owned banks in Indonesia. Design/methodology/approach: The method used in this study uses panel data. The data used are secondary data obtained from Bank publication reports for the period 2007 - 2017. The population used in this study is state-owned bank and sample selection based on purposive sampling. Findings: The results showed that the leverage measured by the DER ratio had a negative and significant effect on the financial performance (ROA) of state-owned banks in Indonesia. The effect of Loan deposit ratio, debt equity ratio and capital adequacy ratio together are still low on the financial performance of state-owned banks in Indonesia. Loan deposit ratio that does not have a real effect on financial performance, it is better if the loan distribution is adjusted to the economic conditions faced. An aggressive credit distribution strategy is not always profitable for banks, especially when in uncertain economic conditions.*

Keywords---*Sustainability, State-owned banks, Financial performance*

Originality/value: This research will be useful in mapping the determinants of state-owned banks performance in Indonesia, focusing on the process of the funding, leverage, capital.

I. INTRODUCTION

Economic changes in the current era of globalization are characterized by very tight business competition, including the national banking market. To deal with competition, a management strategy with high effectiveness results is needed. Strategies need to be developed accurately, firstly, by identifying the capability of banks to compete. At this stage, the early identification of factors which form a competitive strategy becomes crucial (Puspitasari*et al*., 2015). The fact, the internal capability of national banks has not been optimal in keeping up with dynamics and changes in the business environment (Puspitasari and Setiadi, 2016). Measuring the level of management effectiveness is indicated by the ability of banks to benefit. These advantages can be analysed using profitability ratios.

The State-Owned Public Bank is an Indonesian state-owned bank that is included in the IDX list which can provide the state budget contribution with dividends given to the state as the owner of these banks (Diffia, 2015). The strategic role of a State-Owned Bank can be achieved if a State-Owned Bank can operate optimally to create profits. An overview of the ability of a State-Owned Bank to generate profits can be seen from the development of return on assets. Based on financial statements, return on assets of state-owned banks fluctuated during the period 2007 to 2017.

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Werdaningtyas (2012) stated that the fluctuation of the loan portfolio ratio of the State-Owned Public Bank will be in line with changes in bank financial performance (ROA). In conditions, the ability of banks to effectively channel loans will increase bank profits, in line with improving bank performance. The size of the loan deposit ratio (LDR) of a bank will affect the performance of the bank. However, empirical evidence in 2015 and 2017, the increase in the bank's loan deposit ratio, was not accompanied by an increase in ROA, and vice versa. This empirical evidence is not in line with the results of Brigham and Houston research (2009). Previous studies have shown that debt to equity ratio, loan to deposit ratio and capital adequacy ratio as bank specific factors influence return to assets. Research gap are shown in previous studies. Based on the identification of these problems, the researcher aims to obtain empirical evidence regarding the determinants of financial performance of state-owned banks in Indonesia.

II. LITERATURE REVIEW

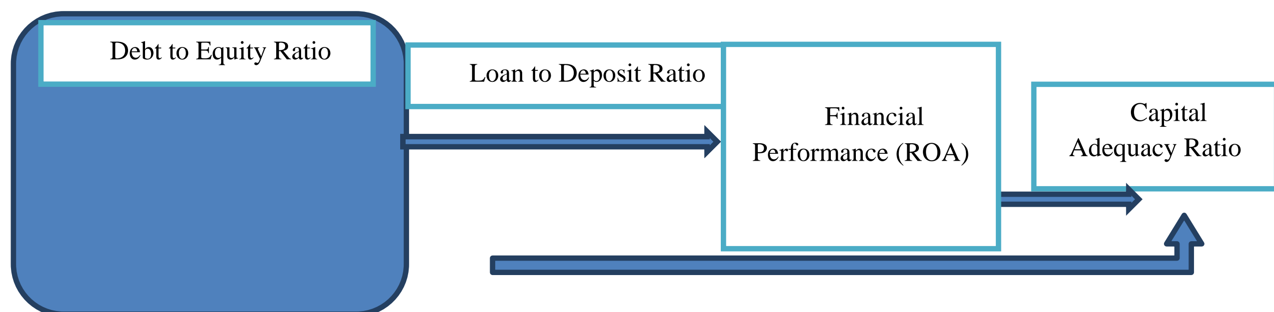
Profit is the ultimate goal of banks. All the strategies designed All the strategies designed and activities performed thereof are meant to realize this grand goal to show excellent financial performance. To measure the financial performance of State-Owned Banks, there are variety of ratios of profitability (Murthy and Sree, 2003; Alexandru *et al*., 2008). This study used Return on Asset (ROA) as a proxy of financial performance.

Funding policies are reflected through the debt to equity ratio (DER) that greatly affects the achievement of profits earned by the company (Saudi, 2018). This ratio shows that every rupiah of its own capital is used as collateral for debt. Brigham and Houston (2009) state that high operating leverage has consequences for changes in income in small amounts and will result in large changes in the company's financial performance. The high debt to equity ratio reflects relatively high risk, resulting in a decrease in return on assets. Maulita and Tania (2018) and Afriyanti (2011) studies found that Debt to Equity Ratio has a negative and significant influence on Return on Assets. The higher the Debt to Equity Ratio will affect the profit achieved by the bank. This shows, the greater a bank gets its funding from debt, the lower the bank's financial performance. Due to the interest expense that must be paid for funding from debt, it reduces the net income of a bank.

Loan deposit ratio is one of the ratios that shows the ability of banks to provide funds to debtors using third party funds. The higher the value of the Loan to Deposit Ratio (LDR) indicates the lower ability of banks to face liquidity risk. Conversely, the lower the ratio of the Loan to Deposit Ratio (LDR) indicates the lack of effectiveness of banks in lending so that there is a loss of opportunity to earn profits. Eng (2012) and Salim (2017) found that Loan to Deposit Ratio has a positive and significant effect on return on assets. The results of this study are different from research of Bernardin (2016), Puspitasari (2016), Fajari and Sunarto (2017), and Masril (2017) who found that Loan to Deposit Ratio have indirect effect to return on assets.

Capital is the amount of own fund available to support the bank's operation and act as a buffer in case of adverse condition and influence profitability (Athanasoglou *et al*., 2005). The greater the capital adequacy ratio, the bank has the ability to provide funds for business and business activities and is able to increase return on assets so as to show good financial performance (Werdaningtyas, 2012). This study are consistent with Sudiyatno and Suroso's research (2010). Different results are shown by the research of Puspitasari *et al*. (2016), Salim (2017), and Fajari and Sunarto (2017) who found that capital adequacy ratios did not affect return on assets.

Based on the results of empirical research, theoretical framework of the study is as follows.



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Based on the above review, the hypothesis proposed is as follows:

H1 : Debt to Equity Ratio has a positive and significant influence on financial performance

H2 : Loan to Deposit Ratiohas a negative and significant influence on financial performance

H3 : Capital adequacy ratio has a positive and significant influence on financial performance

H4: Debt to Equity Ratio, Loan to Deposit Ratioand Capital Adequacy Ratio has significant influence on financial performance

III. METHODOLOGY

The method of this research is descriptive verification, namely research that aims to investigate the effect of capital adequacy ratio, loan to deposit ratio and debt to equity ratio on the financial performance of state-owned banks. The analytical tool used in this research is panel data regression, which is a combination of cross section and time series data.

The data used is secondary data, namely the annual financial statements of state-owned commercial banks. This study used purposive sampling. Purposive sampling is a sampling technique based on the characteristics or consideration of certain criteria of a population (Sugiono, 2014). The sampling criteria used in this study were state-owned banks listed on the Indonesia Stock Exchange which published their financial statements in full during the period 2007 to 2017.

IV. RESULT AND DISCUSSION

Regression analysis is intended to test the extent and direction of the influence of independent variables on the dependent variable. The estimation model used is the Fixed Effect (FE) model, which was obtained after conducting the Chow test and Hausman test. The panel data regression results using the Fixed Effect (FE) model are as table 1.

As presented in Table 1, loan deposit ratio, debt to equity ratio and capital adequacy ratio affect the performances of state owned banks with a minimum of 95% confidence level. Based on Table 1, it can be noted that the regression equation formed can be as follows:

$$Y = 8.075297 - 0.013709X_1 - 0.266968X_2 - 0.100539X_3 + e$$

The constant value magnitude of 8.075297 suggests that if a whole independent variables are not considered as influential against financial performance or are constant, then the magnitude of financial performance value is 8.075297. The loan deposit ratio coefficient magnitude of -0.013709 indicates that the bigger the value of loan to deposit ratio the smaller the value of financial performance, and vice versa. Debt to equity ratio coefficient magnitude of -0.266968 indicates a negative relationship between debt to equity ratio and financial performance. It means the bigger the deposit to equity ratio the smaller the value of financial performance, and vice versa. Capital coefficient magnitude of -0.100539 indicates a negative relationship between operation efficiency and financial performance. It means the bigger the value of capital the smaller the value of financial performance, and vice versa (Abdul Hadi et al., 2019).

Table 1:*Data Panel Regression Results*

Dependent Variable: ROA				
Method: Pooled Least Squares				
Sample: 2007 2017				
Included observations: 11				
Cross-sections included: 4				
Total pool (balanced) observations: 44				
Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	8.075297	1.497452	5.392691	0.0000
LDR	-0.013709	0.011235	-1.220210	0.2295
DER	-0.266968	0.075542	-3.534045	0.0010
CAR	-0.100539	0.063522	-1.582761	0.0214
R-squared	0.295708	Mean dependent var		2.907045
Adjusted R-squared	0.242886	S.D. dependent var		1.152749
S.E. of regression	1.003033	Akaike info criterion		2.930443

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Sum squared resid	40.24304	Schwarz criterion	3.092642
Log likelihood	-60.46974	Hannan-Quinn criter.	2.990594
F-statistic	5.598209	Durbin-Watson stat	0.286410
Prob(F-statistic)	0.002657		

The result of debt to equity ratio against financial performance indicates that debt to equity ratio has a negative and insignificant influence on financial performance. It means if the debt to equity ratio declines, it will increase the bank performance which is proxy by the financial performance indicator. It is indicated with the value of t_{value} less than t_{table} with the significance less than 0.05, so that H_1 is rejected. This indicates that most of state owned banks in Indonesia have already kept its debt to equity in safe level. Result of this study is in accordance study of Maulita and Tania (2018) and Afriyanti (2011).

The result showed loan to deposit ratio has a negative influence on financial performance. The result showed that t_{value} less than t_{table} with the significance more than 0.05. This means that the influence of loan to deposit ratio on financial performance is insignificant on the significance level below 5%, or in other words H_2 is rejected. Optimal credit distribution, inconsistent with assuming it will increase profits and financial performance. The loan to deposit ratio of a bank will affect public trust in banks to save their funds. However, this result is inconsistent with Eng (2012) and Salim (2017) which is loan to deposit ratio has positive and significant influence on financial performance.

The result of capital against financial performance indicates that capital has a negative influence on financial performance. It means if the capital declines, it will increase the bank performance which is proxy by the financial performance indicator. It is indicated with the value of t_{value} smaller than t_{table} with the significance less than 0.05, so that H_3 is accepted. Optimal credit distribution, assuming high credit quality will increase profits and financial performance. These results differ from Puspitasari *et al*. (2016), Salim (2017), and Fajari and Sunarto (2017), which indicate that the capital variable insignificant influence on financial performance.

Based on the collective test result using F-test, it is obtained that F-value (5.598209) > F_{table} (2.90) with the significance F (sig-F) 0.002 or less than 0.05. It infers that debt to equity ratio, loan to deposit ratio, and capital collectively give a significant influence on financial performance. So it can be concluded that H_4 is accepted.

V. CONCLUSION

This study expect state-owned banks can maximize their profit and sustainability. State-owned banks do not maximize the income from loans disbursed. This fact is consistent with the results of the Puspitasari dan Harmanto's study (2010) and Puspitasari's study (2015). This is due to the low quality of credit, which adds to the burden on the bank itself. 5 C in the lending process needs to be implied to filter the occurrence of bad credit. The high debt to equity ratio reflects the high risk of the bank, which causes the bank's financial performance to decline. Capital as a buffer from bank operational risk. Fulfillment of capital adequacy, the application of risk management and compliance to implement bank governance are expected to generate high returns for state owned commercial banks so that it can have an impact on the performance of the bank. For further research can be enriched by using other variables not examined in this study.

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