THE COMPARISONS OF BANK FINANCIAL PERFORMANCE BETWEEN GOVERNMENT OWNED AND LISTED BANK IN INDONESIA

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Abstract

This study aims to examine the differences of bank financial performance based on listing status and government ownership. The population of this study is 120 banks in Indonesia in 2011-2013, both listing and non listing bank. Sample used in this study consist of 75 listing banks and non listing banks, not including Islamic Bank and District Development Bank (Bank Pembangunan Daerah-BPD). The data is analyzed using independent sample test. The results show that (1) Non Performing Loan (NPL) rate in non government ownership bank is lower than NPL rate of government owned bank, and (2) NPL rate of listed bank is lower than NPL rate of non listed bank.

Keywords: Financial Performance, Non Performing Loan, Listing Status, Government Ownership

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1 Introduction

The aim of this study is to examine the differences of financial performance (non performing loan-NPL) betweeenthe government ownership and non government ownership banks, and the differences of financial performance between listed and non listed banks.

NPL is the failure in credit. The high ratio of NPL faces by a bank will cause difficulties for the bank to develop loan portfolio and financing a new profitable loan. The high ratio of NPL can weaken and reduce the chance of growth in the economic sector, private sector, as well as job creation (United States Agency International Development, 2011). NPL acts as an indicator used to assess a bank's failure in credit distribution and the implication of corporate governance (CG) application.

Government ownership of the bank contains social purposes such as prioritize public interest and support the financing activity of less promising business sector that aggravates bank financial performance (Cornett *et al.*, 2009). The government ownership that supposed to motivate the banking growth, cause the inefficiencies in bank financing performance (Berger *et al.*, 2005). The prior study indicates that the government ownership of a certain bank cause a credit risk owned by the bank higher, especially for the countries affted by the Asia (Cheng *et al.*, 2013). Government ownership also causes a decline in bank performance. It is because government motives contains social purposes such as prioritize public interest and support the financing activity of less promising business sector that burden the bank financial performance (Cornett *et al.*, 2009).

In the bank operation there is a conflict of interest between the director and the comissioner, stakeholder or the affiliated party of the director, commissioner or shareholders who might harm the bank (Guidance of Good Corporate Governance/GCG in Banking, 2012). The conflict of interest affects the policies implementation or GCG implementation in the bank (Komite Nasional Kebijakan Governance-national Committee of Governance Policy/KNKG, 2012). The conflict of interest can be controlled with intern and extern mechanism (Babatunde and Olaniran, 2009).

The study conducted by Ahmad and Campus (2013) concluded that private bank positively affect the NPL. Cheng *et al.* (2013) stated that bank ownership structure and listing status of a bank affect bank financial performance. Cornet, Guo, Khaksari, and Tehranian (2009) concluded that state owned bank have a lower profitability, small amount of core capital, and have a higher credit risk compare to private bank. Indonesia bank industry is a highly regulated industry along with a strict regulation of financial management and CG application. Thus the CG application on non listed bank industry of Indonesia is important to be examined.

There are differences of this study and the prior study. This study examines the differences of the government ownership and non government ownership on NPL performance of Indonesia's listed and non listed bank in 2012-2013.

This study constructs a model that can answer these following questions: (1) Are there any

differences of financial performance in the bank with government ownership and the bank without government ownership? (2) Are there any differences of financial performance in the bank status (listed bank and non listed bank)?

2 Literature review

Jensen and Meckling (1976) defined agency relationship as a contract involving one or more people (principals) who ask another person (the agent) to organize the company, resulting in the delegation of decision-making authority from the principal to the agent. If both parties maximizing their own interests, then the agent will not provide the best performance for the principal benefit, while the principal may restrict the possibility of applying incentives for agents in accordance with their performance. Thus, the company needs to provide cost to ensure the agents will make a right decision in accordance with the principal's perception. It is explained that the agency cost will occurs when the principal and agent itself have some conflict of interest and when the principal face some difficulties in controlling the agent.

As the corporate organizer, manager tends to have more internal information and understand company future prospect better than the stakeholder, thus the manager needs to inform the current condition of the company to the owner. Sometimes the information are not significant with the real condition, these kind of informations are named information asymmetric (Ujiyantho and Pramuka, 2007). The asymmetric information can be a conflict trigger of stakeholder and manager.

The manipulation conducted by manager which started by conflict of interest can be minimized with certain monitoring mechanism to align the current interests. The alignment mechanism can be done by widening the managerial ownership (Jensen dan Meckling, 1976), company stocks owned by institutional investors (Colpan *et al.*, 2007), and the monitoring process perform by board of directors (Ujiyantho and Pramuka, 2007).

Managerial ownership aims to surpress the conflicts between managers and external stakeholders (Adnan *et al.*, 2011). Institutional ownership take some roles in company monitoring along with these kind of reasons: (1) institutional ownership own the majority of company stocks, (2) the high rate of investation profit potential, (3) institutional ownership has less ability in financing stocks without affecting its price, (4) has the strong impact for the management, (5) has the fiducia responsibility to the company owner, and (6) has the ability to monitor the executive performance. Board of director take some roles in company operation by control the top management activities and controlling company resources and operational activity (Pandya, 2011). The relationship of stakeholder and manager is the real definition of agency relationship, thus the issue "separation of ownership and control" can be stated as the common issue of agency problem (Jensen and Meckling, 1976), thus it can be concluded that agency cost can develop the ownership structure of the company.

There are other perspectives of ownership structure based on company stakeholder numbers, they block ownership and dispersed ownership (Adnan *et al.*, 2011). Block ownership is the condition when the party owned company stocks more than five percent (dispersed ownership). Block owners tend to put more attention on company performance than individuals who own stocks less than 5% (dispersed ownership). Dispersed ownership owned fewer portions of the stocks, thus they have a lower motivation to monitor the company than the block owners did. The block holder will monitors manager's performance more thoroughly and hold a power to affect board decision taking process. Thus, the existence of block holder can positively affect company performance that realized through the achievement of low capital cost and monitoring effectiveness (Dwivedi and Jain, 2005).

This study focuses on institutional ownership by examining the differences of bank financial performance in government owned bank and public bank, as well as the differnces of financial performance in listed bank and non listed bank.

2.1 Corporate governance

CG is defined as an environment developed by trust, ethics, and moral value that represent synergic effort from related parties (Crowther and Seifi, 2011). According to the simple finance model concept, or commonly knowned as agency theory, the main problem of CG is constructing the regulations and incentives in order to effectively align agent's behavior according to principal's interest. It is assumed that agent (manager) is an untrusted person, have their own interest and opportunistic behavior, thus CG that can protect principal's interest and control the agent's behavior is needed (Jensen and Meckling, 1976).

There are two mechanisms that can be used to create good governance, they are: internal mechanism and external mechanism (Babatunde and Olaniran, 2009). Internal mechanism includes: ownership structure, board of directors, managerial compensation, financial transparency, and impartial information disclosure (OECD, 2005). The internal mechanism form ussually are used to regulate the problems related to: board composition, internal structure, decision making process, disclosure requirement, and compensation-incentives. External mechanism is a technique based on market that designed to strengthen the internal governance structure, outlined in the regulations and legislation with the aim of creating operational efficiencies for the company, whether in internal and external environments (OECD, 2005). The other internal

mechanisms are developed by national or international instituton in the best practice (disclosure quality, audit and accounting standard, employee regulation, standard environment, industry product standard, and listing requirement).

CG mechanism used in this study are (a) internal mechanism, in this case ownership structure. Ownership structure is the structure of company ownership sharing focused on the broad role of stockholders, thus they can control company management (Chen, 2001). The proxy used to measure the ownership structure is government ownership. Government ownership is government involvement in the business sector realized with the company ownership for a certain purposes, among others is privatization interest to restructure and ensure the viability of an institution (Ghozali, 2013). (b) the external mechanism is a bank listing status. Go Public is a bank effort in socializing their company by accepting the public funds inclusion, whether in ownership term or establishment of company management policy. The capital market has an important role in extern mechanism. The capital market is continuously monitoring and put an objective value for the company or even for the company management. The company stock performance is a transparency value of public perception on company value for manager and owner. The measurement can be used by the stockholders to assess manager's performance and as a consideration in providing incentives for managers

Bank with government ownership is less monitored by their owner because the owner believes that the bank will be strictly monitored by the government. Less supervision performed by the owner leads the bank to face more risk and likely to be bailed out by the government when a crisis take place. It is then become a cause for the manager to put less effort in improving the bank performance. (Cheng *et al.*, 2013). Berger *et al.,* (2005) stated that government owned banks tend to have low efficiency and high rate of NPL because government ownership will reduce the credit access, reducing financial development system, and restraining the economic growth. Cornett *et al.* (2009) stated that state-owned bank has low profitability, less main capital, and higher credit risk compared with non-state owned bank. The differences of government ownership can affect bank performance (Berger *et al.*, 2005; Cornett *et al.*, 2009; Cheng *et al.*, 2013). Thus, the first hypothesis can be formulated as:

H1: There are differences in financial performance of bank with government ownership and bank without government ownership.

The bank listing status can improve the asset quality and capital adequacy ratio. The bank listing can affect the risk taking process of the bank because the listing bank will have more strict regulation compare to non listing bank. The bank listing status is also able to realize the bank capital that can be reached with lower costs (Cheng *et al.*, 2013). Listed bank can developed faster, using less financial leverage, investing less in intangible assets, and generate smaller returns compare to non listed bank (Capasso, Rossi, and Simonetti, 2006). The differences in the level of risk taking in turn affects the difference in the bank financial performance (Capasso *et al.*, 2006; Claessens and Tzioumis, 2006; Petranov, 2006; Cheng *et al.*, 2013). Thus, the second hypothesis can be formulated as:

H2: There are differences in financial performance of listed bank and non listed bank.

3 Research method

This study population is all banks in Indonesia in 2011-2013, both listed and non listed bank. The total number of banks in Indonesia is 120 banks; consist of 36 listed banks and 84 non listed banks. The sample used in this study is 225 banks (consist of 75 listed banks and non listed banks in 2011-2013) selected using purposive sampling technique. The purposive sampling technique is a non probability sampling with a certain criteria (Sekaran and Bougie, 2013). The selected sample criterias are a: (1) non Islamic banks dan non district development banks operated in Indonesia in 2011-2013, (2) the banks issued annual report of 2011 to 2013 which can be accessed by authors, (3) there are ownership structure and bank listing status related data that becomes main focus of this study, either in the annual report or other publicity reports.

This study used independent sample test analysis. Data used in this study is a secondary data taken from company annual report in 2011-2013.

4 Analysis result

The first hypothesis examines whether there are financial performance differences of bank with government ownership and bank without government ownership. The hypothesis testing results can be seen below:

Table 1. T-test of Government Owned Bank-Non Government Owned Bank-1

Government Ownership	Notation	N	Mean
NPL of Government Ownership Bank	1	22	-0.032
NPL of Non Government Ownership Bank	0	201	-0.016

Notes: 1 = Government ownership bank
0 = Non government ownership bank

According to the Table 1, it can be seen that the average NPL of government ownership bank is -0.032, meanwhile the average NPL of non government ownership bank is -0.016, the value indicates that the NPL of government owned bank is different with the NPL of non government owned bank. The results of independent sample t test can be shown as:

Table 2. T-test of Government Owned-Non Government Owned-2

Notes		Levene's Test for Equality of Variances		t-test for Equality of Means	
		F	Sig.	t	Sig. (2-tailed)
NPL	Equal variances assumed	0.982	0.323	-4.44	0.000

According to the Table 2, it can be seen that F count of Levene's Test is 0.982 with the probability of 0.323 (>0.05%). It indicates that both of the banks share a same variance. Then, seen from the output of equal variance assumed which showed the t value in the amount of -4.44 with the significance probability of 0.000 (<0.05), the value showed that NPL of government owned banks are different with NPL of non government owned banks (H1 is accepted).

The t-test results in Table 1 and 2 show that the average value of NPL of government owned banks are greater than the average value of NPL of non government owned banks, with the significance rate at the amount of 0.000 (0%). It shows that government owned banks have worse financial performance compared to non government owned banks. This condition indicates that the government owned banks have a high NPL rate. It shows that the government owned banks have a higher credit distribution failure rate compared to the non government owned banks.

The second hypothesis examines whether there are differences of financial performance of listed bank and non listed bank. Below is the result of the second hypothesis testing:

Table 3. T-test of Listed Bank-Non Listed- Bank 1

Government Ownership	Notasi	N	Mean
NPL Listed Bank	1	106	-0.021
NPL Non Listed Bank	0	117	-0.014

Notes: 1 = Listed bank
0 = Non listed bank

According to the group statistics table above, it can be seen that the average NPL of listed bank is -0.021, while the average NPL of non listedbanks is -0.014, the values indicate that the NPL of listed banks and non listed banks are different. However, the independent sample t test is still needed.

Table 4. T test of Listed Bank - Non Listed Bank-2

Notes		Levene's Test for Equality of Variances		t-test for Equality of Means	
		F	Sig.	t	Sig. (2-tailed)
NPL	Equal variances assumed	1.418	0.235	-3.366	0.001

Independent samples t test table showed that F count of Levene's Test is 1.418 with the probability in the amount of 0.235 (>0.05%). It is shown that both of the banks share the same variance. It can be seen from the output of equal variance assumed t value is -3.366 with the significance probability at 0.001 (<0.05). The value means that the NPL of listed banks and non listed banks are different (H2 is accepted).

According to the t test result it can be seen that the average NPL of listed banks is smaller than the average NPL of non listed banks with the significance level of 0.001 (0.1%), thus it can be concluded that the performance of listed banks (NPL= -0.021) are better than the performance of non listed banks (NPL= -0.014). This condition usually takes place in listed banks owned by block holder/block ownership. Block ownership controls company performance more than dispersed ownership, because the dispersed ownership is lack of motivation in monitoring the managers (Jensen and Meckling, 1976). Block holder in the listed banks will perform more control to the company, thus company performance can be improved.

5 Discussion

The results show that the performance of government owned bank is worse than the performance of non government owned bank. It is because the government owned bank is likely to be bailed out by the government when a financial crisis occurs. In response, the managers of government owned bank

put less effort in improving the bank performance. (Cheng *et al.*, 2013). As the result, the performance of government owned bank is worse than the performance of non government owned bank.

This statement is supported by Ianotta *et al.* (2012). They stated that the failure risk of government owned bank is lower than the failure risk of non government owned bank. However the failure risk does not indicate that the operational risk will be low. The operational risk also can not reflect a good economic and financial condition of the bank. It is caused by government support in the form of protection mechanism.

The mechanism is a benefit for state owned bank because it provides a lower cost of capital. However the protection does not affect market order and provide an opportunity for the market to improve the risk taking. Thus, while having a low risk of failure, government ownership pose a high operational risk, as an illustration, the economic and financial conditions are worse than the non government ownership bank.

The analysis result is in a line with the study conducted by Ahmad and Campus (2013). They stated that dispersed ownership can reduce bank performance and improve the bank risk. Bank with listing status, dispersed ownership, and less managerial control from the owner, will lead to the assymetric information and conflict of interest between the owner and managers. (Jensen and Meckling, 1976). It leads to the decision taken will be more benefiting for the managers. Lack of supervision and managerial control can lead managers to take high risks in the loan portfolio with the aim of improving the efficiency of short-term costs through lending to low quality debitors, which can increase the future NPL rate. This analysis result supports the statement that listed bank performance (with block ownership composition) is better than non listed bank performance (with dispersed ownership composition).

6 Conclusion

This study aims to explain the differences of bank financial performance in government owned banks and non government owned banks, and also the differences of bank financial performances in listed status banks and non listed status banks in Indonesia. The study results indicate that:

1. NPL rate of non government owned bank is lower than the NPL rate of government owned bank. It means that the bank financial performance of non government owned bank is better than the bank financial performance of government owned bank. It is because the government ownership of the bank is followed by political interest, thus the government program will not provide benefit for the bank.
2. NPL rate of listed bank is lower than the NPL rate of non listed bank, it indicates that the bank financial performance of listed bank is better than the bank financial performance of non listed bank. It indicates that block holder ownership in the listed bank has positive effect to the bank financial performance.

7 Suggestions

According to the research result, below are the suggestions that can be given:

1. The research result showed that the bank financial performance of non government owned bank is better than the bank financial performance of government owned bank. This results indicates the need to review the government ownership in the bank to reduce government involvement in the bank operations, that leads to the poor performance of bank.
2. The needs to divide the stock ownership into some block holder ownerships in order to avoid dispersed ownership, which leads to less supervision and monitoring of bank management. As the result, bank performance faces an inefficiencies.
3. The main suggestion that can be given are to develop a supervision regulation related to ownership structure, perform a more strict monitoring of credit allocation process, thus the common guidance of risk management can be gained, for example risk governance.

8 Research limitation

The limitations of this study are:

1. This study is conducted in a short period (2011-2013). Thus, the analysis result that can be given is not precise enough.
2. The variabels used in this study are only ownership structure and bank listing status. In the future, other studies can develop the research with other variabels, such as capital structure or managerial remuneration, in order to examine the result consistency of bank financial performance.

9 Research result impication

9.1 Theoritical implication

The result can improve the understanding of ownership structure of bank management in Indonesia. The result is supporting the statement which stated that the bank financial performance of non government owned banks and listed banks are better than the bank financial performance of government owned bank and non listed bank.

9.2 Managerial implication

By implementing good corporate governance, the bank financial performance is expected to be improved (measured by a low rate of NPL). A low rate of NPL showed a low rate of credit distribution failure, which means that the bank success

opportunity is pretty high. Thus it will attract more investor to invest in Indonesian bank. This condition will support the bank function of financial intermediation organization that will prop other industrial sectors. In the end bank industry will support the national economic.

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