

# Factors That Affect the Financial Performance of Family-Owned Manufacturing Companies Listed in Indonesia Stock Exchange

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## ABSTRACT

This study aimed to obtain the empirical evidence about the effect of Good Corporate Governance (GCG) on financial performance with Net Working-Capital Turnover as a mediating variable among family-owned manufacturing companies listed in Indonesia Stock Exchange in the period of 2016 - 2018. This study used the purposive-sampling method with a total sample consisting of 93 data. The software used for data processing technique is bootstrapping with Smart PLS 3.0. The result indicates that Good Corporate Governance does not affect Net Working-Capital Turnover. The results also indicate that Institutional Ownership, the Board of Commissioners, and Committees positively influence Financial Performance. This study also shows that the General Meeting of Shareholders and Net Working-Capital Turnover does not affect Financial Performance.

**Keywords:** *Good Corporate Governance (GCG), Net Working Capital Turnover, Financial Performance*

## 1. INTRODUCTION

Every company wants to show good performance in implementing and using the correct financial practices. The company's performance in financial terms is assessed from the qualifications and efficiency in operating the financial statements in one period in accordance with applicable standards.

One of the factors influencing financial performance in a company is Good Corporate Governance (GCG). Indonesia started implementing corporate governance in 1997 during the economic crisis. In Indonesia, the way of implementing corporate governance is still relatively weak. One of the causes of the crisis is because it does not meet the conditions of adequate corporate management, and there is no clear division of tasks. Elements in the corporate governance consist of Institutional Ownership, Board of Commissioners, General Meeting of Shareholders, and the overall size of the Committee, both the Audit Committee and the Nomination and Remuneration Committee as stipulated in Law No. 40 of 2007 [5] concerning the Limited-Liability Companies.

The implementation of working capital is essential for every company. The availability of working capital must be adequate to finance the company expenses or operations every day, because adequate working capital enables the company to operate effectively and efficiently so that it will not experience any financial difficulties. Company leaders must maintain the implementation of good working-capital management so that the amount of working capital is balanced. The application of working capital is carried out with a rotation of net-working-capital.

## 2. LITERATURE REVIEW

According to [8], the elements of Agency Theory through property rights and financial theory develop the theory of ownership structures for corporate businesses. The agency relationship arises when the capital owner assigns an agent the duty to provide a service and is responsible for the authority to make operational decisions related to the agreed work-contract.

**Signalling Theory.** [1] promoted Signalling Theory, a concept in which the information provider can choose what and how the information is displayed, and the information receiver can choose how to interpret it.

**Financial Performance.** According to [3], financial performance is one of the analytical methods used by companies to measure the effectiveness and compliance by using financial rules as a basis for the good and correct financial practices. Another concept of financial performance is mentioned by [11], which defined it as the result or achievement from the company's management effectively during a certain period.

**Good Corporate Governance (GCG).** According to SOE Ministerial regulation set forth in the Letter number: PER-001 / MBU / 2011 Article 1 regarding the implementation of good corporate governance in State-Owned Enterprises [6], the notion of GCG is the principles that underlie a process and processing mechanism companies based on the laws and business ethics. [2], on the other hand, argued that GCG is a

structure and process to ensure that the principle of migrating tariffs becomes a culture, directing and controlling companies to achieve sustainable growth, increasing added-value, while taking into account the balance of stakeholders' interests in accordance with the written corporate principles and applicable laws and regulations.

**Institutional Ownership.** According to [12], institutional ownership is a situation in which an institution has a stake in a company. The institution can be in form of government institutions, private company institutions, domestic and international institutions who have the family-ownership background.

**Board of Commissioners (BoC).** According to the Law on Limited-Liability Company Number 40 Year 2007 [5], the Board of Commissioners is a part of a company responsible for overseeing and providing the advice to Board of Directors (BoD) and ensuring that the company runs good corporate governance practices. The Board of Commissioners is appointed by the General Meeting of Shareholders (GMS).

**General Meeting of Shareholders (GMS).** According to the Law Number 40 Year 2007 concerning the

Limited-Liability Companies in Article 1 Paragraph (4) [5], the General Meeting of Shareholders (GMS) is a part of a company that has the authority which is not given to the Board of Directors or Board of Commissioners within the limits specified in this law and / or articles of association.

**Committee.** According to the Law Number 40 Year 2007 concerning the Limited-Liability Companies under Article 121 [5], the BoC may form a Committee whose members are one or more members of the BoC. The company's function is to make committee positions to support the work of the Board of Commissioners. The committee itself will be responsible for the Board of Commissioners in providing input in formulating company policy.

**Net-Working-Capital Turnover.** [10] stated that Net-Working-Capital Turnover is a ratio showing the relationship between working capital and sales, and shows how much sales (in Rupiah) the company can generate for each Rupiah spent for working capital.

The Conceptual Framework in this research is displayed as follow.

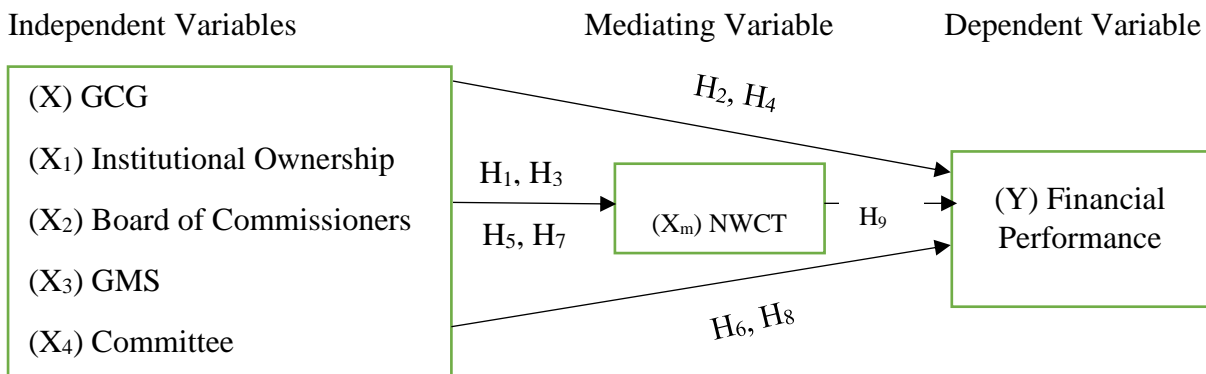


Figure 1 Conceptual Framework

Based on the research framework, the hypotheses in this study were formulated as follows:

H<sub>1</sub>: Institutional Ownership positively and significantly influences Net-Working-Capital Turnover.

H<sub>2</sub>: Institutional Ownership positively and significantly influences Financial Performance.

H<sub>3</sub>: The Board of Commissioners positively and significantly influences Net-Working-Capital Turnover.

H<sub>4</sub>: The Board of Commissioners positively and significantly influences Financial Performance.

H<sub>5</sub>: The General Meeting of Shareholders positively and significantly influences Net-Working-Capital Turnover.

H<sub>6</sub>: The General Meeting of Shareholders positively and significantly influences Financial Performance.

H<sub>7</sub>: The Committee positively and significantly influences Net-Working-Capital Turnover.

H<sub>8</sub>: The Committee positively and significantly influences Financial Performance.

H<sub>9</sub>: Net-Working-Capital Turnover positively and significantly influences Financial Performance.

### 3. RESEARCH METHOD

The dependent variable in this research is Financial Performance, which uses the Return-on-Equity (ROE) calculation. Meanwhile, the independent variable is GCG, which consists of Institutional Ownership, the BoC, GMS, and Committees. The mediating variable in this study is the Net-Working-Capital Turnover. The subject of this research is manufacturing companies listed in the Indonesia Stock Exchange (IDX) from the year 2016 to 2018 of which the data was acquired through the IDX website: [www.idx.co.id](http://www.idx.co.id) [15], with family business as the object of this research. The

purposive-sampling technique was used in this research, whereas the sampling is done non-randomly by determining specific characteristics that are in accordance with the research objectives. The samples in the study consist of 31 companies.

The operational variables in this research are Financial Performance, GCG consisting of Institutional Ownership, the BoC, GMS, Committees, and NWCT. Financial performance as the dependent variable is measured using the Return-on-Equity (ROE) calculation. The formula for calculating ROE is as follow:

$$ROE = \frac{\text{Net Income After Tax}}{\text{Total Equity}}$$

Net-Working-Capital Turnover, that serves as a mediating variable, can be formulated as follow:

$$NWCT = \frac{\text{Net Working Capital}}{\text{Cash Flows From Operating Activities}}$$

$$\begin{aligned} \text{Net Working Capital} \\ &= \text{Current Assets} \\ &- \text{Current Liabilities} \end{aligned}$$

The independent variable in this study is Good Corporate Governance (GCG) or what is called corporate governance. In the implementation of GCG, there are four governance structures examined, namely Institutional Ownership, the Board of Commissioners, General Meeting of Shareholders, and Committees. The formula of each independent variable is explained below.

Institutional Ownership can be formulated as follow:

$$\text{Institutional Ownership} = \frac{\text{Number of Institutional Shares}}{\text{Number of Shares Outstanding}}$$

The Board of Commissioners can be formulated as follow:

$$\text{Board of Commissioners} = \text{Number of members of BoC}$$

The General Meeting of Shareholders can be formulated as follow:

$$\text{GMS} = \text{Number of meetings of BoD and BoC}$$

The Committees can be formulated as follow:

$$\text{Committees} = \text{Number of members of Committee}$$

The data used in the study does not need to carry out the classical-assumption tests. They are classified as non-parametric types and have predictive relationships between the constructs. In addition, the sample size is not too large, so bootstrapping does not require a minimum sample size. In data processing using Smart PLS 3.0, it has included indirect calculations that are useful in analyzing the power of mediation variable that are related to the independent variables and the dependent variable.

#### 4. DATA ANALYSIS

A descriptive statistics test is a method used to analyze and present the quantitative data that aims to describe the data so that it is easy to understand. Descriptive statistical tests consist of Mean (average value), Median (middle value), Minimum (minimum value), Maximum (maximum value), Standard Deviation (standard deviation), Excess Kurtosis (spiky), and Skewness (inclination).

The descriptive statistical results for the 2016-2018 period data show that financial performance has a mean value of 0.123, a median of 0.108, a minimum value of 0.002, a maximum value of 0.406, a standard deviation value of 0.081, excess kurtosis of 1.685, and skewness of 1.075. Net-Working-Capital Turnover has a mean value of 8.387, a median of 2.442, a minimum value of -20.267, a maximum value of 273.608, a standard deviation of 33.813, excess kurtosis of 46.047, and skewness of 6.525. Institutional ownership has a mean value of 0.623, a median of 0.680, a minimum value of 0, a maximum value of 1, a standard deviation value of 0.263, excess kurtosis of 0.352, and skewness of -1.069. The Board of Commissioners has a mean value of 4.484, a median of 4, a minimum value of 2, a maximum value of 12, a standard deviation value of 2.046, excess kurtosis of 1.915, and skewness of 1.460. The General Meeting of Shareholders has a mean value of 1.191, a median of 1, a minimum value of 0, a maximum value of 3, a standard deviation of 0.554, excess kurtosis of 0.791, and skewness of 0.436. The Committee has a mean value of 4.409, a median of 3, a minimum value of 2, a maximum value of 12, a standard deviation value of 1.990, excess kurtosis of 5.161, and skewness of 2.037.

Structural Model Test was done by moving the Microsoft-Excel data to Smart PLS 3.0. After being moved, the data was connected to the data path and linked from one variable to another.

The test of validity and reliability was done using a measurement model (outer-model) consisting of exogenous and endogenous measurement model. An exogenous measurement model is for the scope of independent latent variables, while the endogenous measurement model is for the scope of mediated latent variables and latent dependent variables. The Cronbach's Alpha value is more than 0.5, which turns out to meet the requirements. The Rho\_A or composite

reliability has fulfilled more than 0.6 requirements. The Composite Reliability qualifies > 0.7, thus the results are reliable. The multiple coefficient-of-determination test results is related to structural-model testing. The adjusted R<sup>2</sup>

result for NWCT and Financial Performance of 0.072 and 0.141, is smaller than R<sup>2</sup> because the ability of the independent variables in this study is very limited.

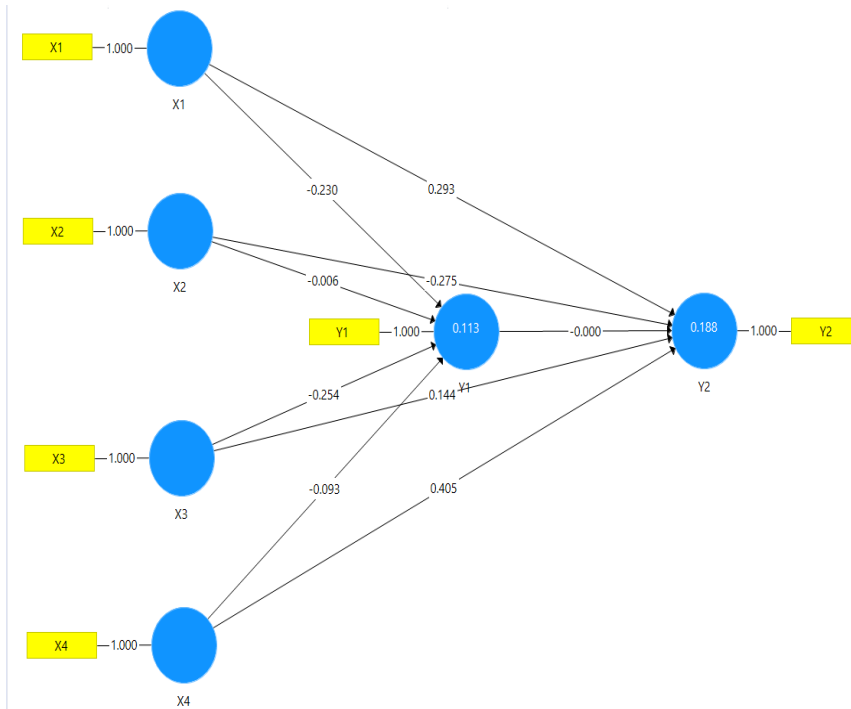


Figure 2 The Estimated-Model Test-Result with R-Square

Table 1 t-Test Results

|                                 | O      | M      | STDEV | t Stats | p-Values | Decision                |
|---------------------------------|--------|--------|-------|---------|----------|-------------------------|
| X <sub>1</sub> → Y <sub>1</sub> | -0.230 | -0.205 | 0.177 | 1.302   | 0.193    | H <sub>1</sub> rejected |
| X <sub>1</sub> → Y <sub>2</sub> | 0.293  | 0.284  | 0.096 | 3.052   | 0.002    | H <sub>2</sub> accepted |
| X <sub>2</sub> → Y <sub>1</sub> | -0.006 | -0.003 | 0.064 | 0.088   | 0.930    | H <sub>3</sub> rejected |
| X <sub>2</sub> → Y <sub>2</sub> | -0.275 | -0.279 | 0.111 | 2.469   | 0.014    | H <sub>4</sub> accepted |
| X <sub>3</sub> → Y <sub>1</sub> | -0.254 | -0.240 | 0.142 | 1.788   | 0.074    | H <sub>5</sub> rejected |
| X <sub>3</sub> → Y <sub>2</sub> | 0.144  | 0.147  | 0.127 | 1.133   | 0.258    | H <sub>6</sub> rejected |
| X <sub>4</sub> → Y <sub>1</sub> | -0.093 | -0.102 | 0.061 | 1.525   | 0.128    | H <sub>7</sub> rejected |
| X <sub>4</sub> → Y <sub>2</sub> | 0.405  | 0.408  | 0.093 | 4.364   | 0.000    | H <sub>8</sub> accepted |
| Y <sub>1</sub> → Y <sub>2</sub> | -0.000 | 0.001  | 0.064 | 0.007   | 0.994    | H <sub>9</sub> rejected |

Source: Data Analysis Results (2020)

The mediation-test results aim at finding out the influence of mediating variable toward the effect of independent variables on the dependent variable. The

results of these mediation tests were carried out by doing Sobel calculations through online system at [www.danielsoper.com](http://www.danielsoper.com) [14].

Table 2 Online Mediation Calculation Results

| Causality Relationship          | Estimate   | S.E.        | Sobel-Test Result | Decision     |
|---------------------------------|------------|-------------|-------------------|--------------|
| X <sub>1</sub> → Y <sub>1</sub> | (a) -0.230 | (SEa) 0.177 | 0.000             | No Mediation |
| X <sub>2</sub> → Y <sub>1</sub> | (a) -0.006 | (SEa) 0.064 | 0.000             | No Mediation |
| X <sub>3</sub> → Y <sub>1</sub> | (a) -0.254 | (SEa) 0.142 | 0.000             | No Mediation |
| X <sub>4</sub> → Y <sub>1</sub> | (a) -0.093 | (SEa) 0.061 | 0.000             | No Mediation |
| Y <sub>1</sub> → Y <sub>2</sub> | (b) -0.000 | (SEb) 0.064 |                   |              |

Source: Data Analysis Results (2020)

## 5. DISCUSSIONS

First, the partial-test results show that Institutional Ownership negatively but not significantly affects Net-Working-Capital Turnover. This is due to the large amount of short-term debt that has not been repaid and has an effect on current assets, especially in the circulation of operational cash-flows. Hence, the shareholders will have difficulty in managing the company, and the cash-conversion-cycle is shorter than that of other companies, because it is not good in the corporate governance system.

Second, the results of this study indicate that Institutional Ownership positively and significantly affects Financial Performance. The commitment between the company and shareholders goes well and can save financial performance in the company.

Third, the results of this study indicate that the Board of Commissioners negatively but not significantly affects Net-Working-Capital Turnover. It means that the joint meetings between the BoC and the BoD, who have policies in making decisions, is ineffective. In addition, coordination on corporate governance is still so weak that it does not produce optimal policies and impact on the company's operations.

Next, the results of this study indicate that the Board of Commissioners positively and significantly influences Financial Performance. It also influences the number of BoC, which has many members, so that it is easy to determine the policies and make good management decisions and coordination. All policies and decisions taken will affect the results of the financial statements. The result of this study also indicate that the General Meeting of Shareholders negatively but not significantly affects Net-Working-Capital Turnover. It means that the meetings run by the company are ineffective and do not match the results of meetings that have been conducted. The application of corporate governance in the management control system is still weak, because the results of board meetings have been conducted routinely, but only monitor the ability of board members in terms of work management.

After that, the results of this study indicate that the General Meeting of Shareholders negatively but not significantly affects Financial Performance. It proves that the role of Board of Commissioners in supervising the Board of Directors by providing advice in decision making has not been appropriately implemented. There are still many members of the BoD who have different goals in carrying out their duties. This difference will have an impact on the company's financial performance which is not increasing.

Concerning the Net-Working-Capital Turnover, the results of this study indicate that the Committee negatively but not significantly affects this variable. The Committee does not run the role effectively and efficiently in carrying out the working-capital management. A large number of Committee members will be ineffective in carrying out the tasks assigned by the BoC.

Regarding financial performance, the results of this study indicate that the Committee positively and significantly influences this variable. The company's

policy is making the Committee facilitates the company in making decisions. The Committee divisions in the company are essential; at least there is an Audit Committee that examines the company's financial statements for each period.

We can conclude the following study results that Net-Working-Capital Turnover negatively but not significantly affect Financial Performance. The working-capital management is very ineffective for the company in long-term. If the cash flow is not effective, then the amount of cash available is not enough to support the sales volume.

Finally, the Mediation-Test results using the Sobel calculations show that the independent variables do not have a mediation relationship. We can conclude that the corporate governance implementation in managing the cash-conversion-cycle is still weak. There needs to be a clear division of tasks so that the company's management control system can run well.

## 6. CLOSING

### 6.1. Conclusions

This research concludes that Institutional Ownership, the BoC, the General Meeting of Shareholders, and Committees negatively but not significantly affect Net-Working-Capital Turnover. The test results of Institutional Ownership, the BoC, and the Committee show that they positively and significantly impact Financial Performance. In contrast, the General Meeting of Shareholders and Net-Working-Capital Turnover has a negative but not significant effect on Financial Performance. The Mediation-Test results using an online calculator (Sobel's calculation) provided in the website: [www.danielsoper.com](http://www.danielsoper.com) show that the independent variables have no mediation relationship.

### 6.2. Limitations

Based on the conducted research and the conclusions, this research still has some limitations. The limitations in this research are: (1) The independent variable used is only the Good Corporate Governance, which only affects the Financial Performance and the mediating variable of Net-Working-Capital Turnover; (2) The period used in this research is very limited, namely from the year 2016 to 2018, so this research only describes the condition of three years; (3) This research only focused on manufacturing companies listed in the IDX and the object of this research is a family business.

### 6.3. Suggestions

Based on the limitations that have been disclosed, we can suggest further research that subsequent researchers can carry out, namely: (1) Use the more extended research period (longer than three years); (2) Add more independent variables related to financial performance and mediation variables in the form of

specific and detailed Net-Working-Capital Turnover; (3) Add other-sector companies such as mining, plantations, and others; (4) Add more sample size of the variables that have a significant influence in previous research.

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