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DO CORPORATE GOVERNANCE AND BANK-SPECIFIC FACTORS MATTER ON BANKING FINANCIAL PERFORMANCE?

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ABSTRACT

Purpose: *This study explores and presents empirical evidence on the influence of self-assessment of bank corporate governance and bank-specific factors on the financial performance of commercial banks in Indonesia.*

Methodology/approach: *We conducted the study on 35 Indonesian public banks listed on the Indonesia Stock Exchange from 2017 to 2021. Using structural equation modeling, a thorough analysis was performed on a dataset of 160 observation samples that were carefully selected through purposive sampling.*

Findings: *This study found that the implementation of corporate governance, which is proxied by the rating of self-assessment of corporate governance, and bank-specific factors significantly affect bank financial performance. The better the corporate governance self-assessment rating, the better the bank's financial performance. Other results indicate that bank-specific factors, as reflected by bank ownership, size, and diversification, significantly positively contribute to bank financial performance.*

Practical implications: *This research aims to provide valuable insights that can support the Indonesian Financial Services Authority (OJK) in implementing effective corporate governance practices. It focuses on enhancing risk management, strengthening the bank's internal capacity, and ensuring compliance with regulations to promote best practices in bank management.*

Originality/value: *This study provides new insight by examining the factors influencing financial performance*

in the banking sector, focusing on bank-specific factors and the regulatory aspects of Indonesian banking governance.

KEYWORDS: *bank-specific factors, corporate governance, financial performance*

ABSTRAK

Tujuan: Penelitian ini mengkaji dan memberikan bukti empiris mengenai peran self-assessment tata kelola bank dan faktor-faktor spesifik bank terhadap kinerja keuangan Bank Umum Emiten Indonesia.

Metodologi/pendekatan: Pengujian dilakukan terhadap 35 bank umum Indonesia yang terdaftar di Bursa Efek Indonesia dari tahun 2017 hingga 2021. Dengan menggunakan model persamaan struktural, 160 sampel dari purposive sampling dianalisis.

Hasil: Penelitian ini menemukan penerapan corporate governance yang diproksikan dengan rating self assessment corporate governance, dan faktor spesifik bank berpengaruh signifikan terhadap kinerja keuangan bank. Semakin baik peringkat self-assessment tata kelola bank, maka semakin meningkatkan kinerja keuangan bank. Hasil lainnya menunjukkan bahwa faktor spesifik bank yang tercermin dari kepemilikan, ukuran, dan diversifikasi bank, memberikan kontribusi positif yang signifikan terhadap kinerja keuangan bank.

Implikasi praktis: Penelitian ini berkontribusi dalam mendukung kebijakan Otoritas Jasa Keuangan (OJK) Indonesia terkait penerapan tata kelola korporasi yang baik dengan memperkuat manajemen risiko, kapasitas internal bank, dan kepatuhan terhadap peraturan untuk mendukung praktik terbaik dalam pengelolaan bank.

Orisinalitas/Kebaharuan: Kajian ini memberikan wawasan baru dengan mengintegrasikan pengujian determinan kinerja keuangan dengan mengelaborasi faktor-faktor spesifik bank dan menginternalisasi aspek regulasi tata kelola perbankan Indonesia.

KATA KUNCI: tata kelola perusahaan, faktor spesifik bank, kinerja keuangan bank.

INTRODUCTION

The emergence of new regulations is driven by changes in the business environment, which is becoming increasingly complex and competitive, as well as by stakeholders' demand for a healthy bank. These circumstances will foster an urgency within the banking industry to promptly adjust to evolving dynamics and effectively implement the aforementioned regulations to enhance operational efficiency. Furthermore, the implementation of new regulations is an obligatory requirement that will foster organizational adherence and facilitate their practical implementation. The requirements set forth by the authority and relevant regulators are integral to the establishment of soundness within banks and the enhancement of management and supervision practices. The implementation of governance reforms in bank management has been observed to foster enhanced productivity and the adoption of optimal practices in financial management within institutions. Enhanced bank management efficiency and optimal bank performance can be attained by implementing more through the implementation of stricter regulations, rigorous monitoring, tighter restrictions, increased capital, and the introduction of new reforms (Kale et al., 2015). The Indonesian Financial Services Authority (OJK) has required the assessment of a bank's stability based on OJK Regulation Number 55/POJK.03/2016 (OJK, 2016b) and Bank Indonesia Regulation Number 13/1/PBI/2011 (BI, 2011). This regulation aims to promote adherence to good governance practices within the banking industry, ultimately leading to the attainment of soundness banks. The Indonesian Financial Services Authority can recommend that the bank provide an action plan based on its evaluation of corporate governance implementation. This action plan should provide a clear and concise roadmap for the bank to tackle the current challenges effectively. It should also include a specific timeframe for implementing these corrective measures. Therefore, implementing mandatory regulations will encourage financial institutions to adhere to sound banking practices.

Many previous studies have explored how corporate governance and bank-specific factors impact the financial performance of banks. Based on the research conducted by Lai and Choi (2014), it has been observed that bank governance plays a significant role in enhancing the financial performance of banks in the Asian region. This highlights the importance of strengthening internal control and compliance measures to help management effectively address risks and achieve organizational goals. A study by Basuony et al. (2014) revealed a noteworthy correlation between corporate governance factors, including board size, board activism, and the number of outside directors, and profitability in both conventional and Islamic banks in Arabian Peninsula countries. The researchers used Tobin's Q as a metric to evaluate the financial performance of banks. The research by Ahmed et al. (2020) and Okoye et al. (2020) emphasizes the correlation between corporate governance mechanisms and profitability. Various factors, including the size of the board, ownership structure, gender diversity, and the existence of an audit committee, are positively associated with profitability. These findings indicate that the successful implementation of corporate governance mechanisms can positively impact the financial performance of organizations. Abdallah and Bahloul (2021) conducted a recent study that discovered an intriguing connection between various corporate governance elements, such as the board of directors, audit committee, and Sharia supervisory board, and key financial performance indicators like return on assets (ROA) and return on equity (ROE) in the Menasa region (Middle East, North Africa, and Southeast Asia).

A recent study explored the relationship between factors specific to banks and their financial performance. Various factors influence 19 European banks' profitability, as

highlighted in a recent research study conducted by Kryeziu and Hoxha (2021). These factors encompass the Capital Adequacy Ratio (CAR), liquidity, funding sources, asset quality, Non-Performing Loan (NPL), and economic growth. In their recent study, Ovelar-Fernández et al. (2022) found a fascinating connection between adopting corporate governance (CG) practices and evaluating leverage, liquidity, and credit risk. As per the research conducted by Benvenuto et al. (2021), they have found evidence that the CG index positively impacts financial performance, but only in a banking system characterized by homogeneity. Conversely, in a banking sector characterized by heterogeneity, the CG index does not facilitate the growth of large banks. According to the research conducted by Outa and Waweru (2016), it has been established that the involvement of capital market authorities and regulators in ensuring adherence to good corporate governance (GCG) practices is of utmost significance. The study highlights that conforming to corporate governance principles has a noteworthy and favorable influence on both financial performance and the overall value of a firm. In a recent study by Goel (2018), significant improvements were observed in the effectiveness of corporate governance reform when it came to implementing corporate governance practices in various sectors of the Indian corporate world. However, the study found no significant link between these reforms and financial performance. Previous studies have confirmed that factors specific to banks play a crucial role in achieving optimal financial performance. Factors such as credit growth, allowance for impairment losses, bank diversification, and operational efficiency have been identified as critical factors influencing a bank's financial performance (Ahmed et al., 2021; Basuony et al., 2014).

In addition, various factors, including the size of the bank, its profitability, net profit margin, and ownership aspects, have been discovered to impact a bank's financial performance. In their study, Mahmud et al. (2016) analyzed the factors specific to banks that have a notable influence on their profitability performance. These variables encompass aspects such as capital adequacy, minimal credit risk, effective cost management, and the size of the bank. Assfaw (2018) argued that the banking industry should ensure capital adequacy, optimal liquidity, efficient cost management, and an asset quality base to enhance performance and profitability. Consistent with previous studies, Ariyibi et al. (2020) found that certain factors specific to banks, such as the loan-to-deposit ratio, capital adequacy, and asset quality, significantly influence financial performance. A recent study by Siddique et al. (2021) found that several factors specific to banks, such as the cost efficiency ratio, average loan rate, liquidity ratio, and capital adequacy ratio (CAR), played a crucial role in determining financial performance. These findings indicate that regulators significantly impact interest rates and reduce the non-performing loan (NPL) ratio through strict monitoring measures, including maintaining liquidity in a competitive financial environment. Past research has examined the impact of ownership structure and diversification on a bank's financial performance. Several studies (Agustini & Viverita, 2011; Luu et al., 2020; Zouari & Taktak, 2014) have found that factors such as bank concentration, diversification, ownership structure, and size can all play a role in shaping a bank's financial performance. A recent study by Brahmana et al. (2018) analyzed the annual financial data of Malaysian banks from 2005 to 2015. The research findings suggest that expanding income source diversification has a beneficial effect on bank performance. This study indicates that non-interest income and risk-adjusted performance provide evidence in support of the risk reduction hypothesis and the resource-based view theory.

Prior studies have predominantly depended on indicators to evaluate the impact of corporate governance factors, including board effectiveness, audit committees, and

ownership, on financial performance. These studies (Ahmed et al., 2020; Basuony et al., 2014; Lai & Choi, 2014; Okoye et al., 2020). Despite using different dimensions and proxies, the current assessment of corporate governance does not provide conclusive findings regarding the overall effectiveness of bank governance. Prior research has investigated the influence of different internal and external factors on financial performance within the financial services industry (Ahmed et al., 2021; Ariyibi et al., 2020; Assfaw, 2018; Mahmud et al., 2016; Siddique et al., 2021). However, these studies have used different measures and have produced conflicting findings. The main goal of this study is to fill research gaps by examining Indonesia's banking sector's financial performance determinants. It emphasizes bank-specific characteristics and banking governance regulations. Previous bank financial performance studies tested a few financial performance variables, yielding inconclusive findings. Based on previous research, this study uses composite bank governance scores. It provides a novel perspective by examining the impact of corporate governance and bank-specific factors on financial performance. Bank governance and contextual factors encourage economic growth and bank stability. This study strives to improve Financial Services Authority (OJK) policies by improving bank corporate governance, risk management, and internal capability. This research may encourage optimal bank management. Risk management, corporate governance, and regulatory compliance can help a bank achieve financial stability and sustainability.

Agency theory provides a crucial perspective for understanding the relationship between corporate governance and bank financial performance. Conflicts of interest can arise between the principal, who owns or controls the company, and the management, commonly referred to as the agent, due to their differing objectives and motivations, as suggested by the agency theory. The principal demonstrates a heightened focus on maximizing utility, notably higher returns. At the same time, agents show a strong interest in the rewards they receive for managing the company. Efficient management is essential for reducing agency expenses and enhancing corporate financial performance, ultimately leading to higher share value. Efficiently managing agency costs can significantly enhance the overall economic performance. It is crucial to have effective corporate governance mechanisms in place to motivate managers to prioritize the principal's best interests. In the context of a bank's operations, it is crucial for bank governance to effectively address the various interests of stakeholders beyond shareholders, ensuring fair treatment among them. By implementing good governance practices, banks can establish mechanisms that promote fairness among stakeholders while also considering the interests of shareholders who prioritize the bank's economic performance.

Previous studies have researched the impact of corporate governance and bank-specific factors on financial performance. In their study, Lai and Choi (2014) discovered that bank governance has a favorable effect on the financial performance of banks in the Asian region. This highlights the significance of enhancing internal control and compliance to aid management in promptly addressing risks and attaining organizational objectives. Basuony et al. (2014) found a noteworthy correlation between the corporate governance aspects and profitability of both conventional and Islamic banks in Arabian Peninsula countries. The study focused on variables such as board size, board activism, and the number of outside directors. To analyze this relationship, they used Tobin's Q as a measure of bank financial performance. Recent research by Ahmed et al. (2020) and Okoye et al. (2020) reveals that corporate governance mechanisms, such as board size, ownership, gender diversity, and audit committees, play a crucial role in enhancing profitability. These studies indicate that

the effective implementation of these mechanisms can significantly enhance corporate financial performance. In a recent study, Abdallah and Bahloul (2021) discovered noteworthy findings about the influence of corporate governance on financial success. The study examined many elements of corporate governance, including the board of directors, audit committee, and Sharia supervisory board, and found a substantial and positive correlation with financial success. The evaluation focuses on two crucial metrics: return on assets (ROA) and equity (ROE).

A recent survey by Kryeziu and Hoxha (2021) examined the profitability of 19 European banks and identified several factors that influenced it. These factors included the capital adequacy ratio (CAR), liquidity, funding sources, asset quality, non-performing loans (NPL), and economic growth. Ovelar-Fernández et al. (2022) conducted a recent study that revealed a noteworthy relationship between corporate governance (CG) practices and ratings for leverage, liquidity, and credit risk. The study revealed a negative correlation between these factors. A recent survey by Benvenuto et al. (2021) found that the influence of the CG index on financial performance is only significant in a banking system with a similar structure. Based on the findings, the CG index positively impacts economic performance. However, this effect is only applicable to a uniform banking system. However, it fails to support the expansion of central banks in a diverse banking sector. A recent research by Outa and Waweru (2016) discovered the significant importance of capital market authorities and regulators in ensuring compliance with Good Corporate Governance (GCG). The study emphasizes the considerable impact of following corporate governance guidelines on financial performance and firm value. Goel (2018) conducted a recent study that found that corporate governance reform significantly impacted the effectiveness of corporate governance practices in different sectors of the Indian corporate landscape. However, the study found no noteworthy correlation between corporate governance practices and financial performance.

Several studies conducted in Indonesia have shown that corporate governance positively impacts banks' financial performance (Artiningsih et al., 2011; Wahyudin & Solikhah, 2017). The implementation of corporate governance in the banking system in Indonesia has been found to positively impact financial performance. The regulatory role of Bank Indonesia in providing guidelines for implementing corporate governance has been shown to enhance ratings and improve performance in the banking industry in Indonesia (Artiningsih et al., 2011). Wahyudin and Solikhah (2017) reveal that GCG ratings affect accounting-based financial performance (ROE, ROA, EPS) but do not directly affect market performance and company growth in the short term. Regulators and capital market authorities play a crucial role in fostering compliance with GCG implementation, which positively impacts financial performance and company value. Jebran and Chen (2023) state that specific corporate governance approaches help address COVID-19 pandemic challenges. These strategies ensure the long-term existence of the organization. These strategies include risk management committees, institutional ownership, board independence, investors, and family ownership. Therefore, one could argue that implementing effective corporate governance in financial institutions fosters a positive work environment for banks, ultimately leading to enhanced financial performance. Conversely, limited implementation of corporate governance practices, indicating a lack of effective corporate governance, necessitates improvement to ensure adequate management and oversight, negatively impacting the bank's financial performance. Based on these arguments, the following hypothesis is proposed:

H_1: Corporate Governance affects bank financial performance.

The resource-based view (RBV) theory highlights the importance of a company's resources in influencing its competitive advantage and overall performance. The RBV theory posits that a company comprises various resources and capabilities, which must be strategically managed to attain a competitive edge that will ultimately enhance its financial performance. Concerning the banking finance business, RBV Theory justifies the ability in resource management and managerial ability to have the potential to increase credit market share, diversify services, and efficiency in bank operations so that they can contribute to gaining a competitive advantage in the financial industry and achieving optimal corporate financial performance. In the framework of RBV Theory, one can make a case for the significance of various bank characteristics, including bank type, bank ownership, bank size, audit quality, market share, and diversification. When effectively managed, these factors are considered valuable resources that can give a bank a competitive edge and ultimately enhance its financial performance.

Prior research has provided insights into the correlation between factors specific to banks and their financial performance. Financial institutions can shape and impact certain factors that are unique to them. These factors are internal and stem from the policies and management decisions implemented by the banks(Bandyopadhyay, 2022). In a recent study by Ahmed et al. (2021), the researchers aimed to analyze the banking sector in Pakistan. Their research findings suggest a strong correlation between non-performing loans (NPLs) and bank characteristics such as credit growth, net profit, impairment, and value impairment. Conversely, efficiency, bank size, and asset returns negatively reduce the occurrence of NPLs. One interesting discovery from this study suggests that higher interest rates, exchange rates, and political risk are linked to a rise in non-performing loans (NPL). At the same time, gross domestic product (GDP) negatively correlates with NPL. Chaity and Islam (2022) investigated how corporate governance principles affect Dhaka Stock Exchange-listed commercial banks' operational efficiency and earnings management. The study covered 2007–2016 in Bangladesh. The study found that corporate governance guidelines reduced earnings management. This means fewer conflicts of interest, better shareholder protection, and less self-serving banking management. According to a 2019–2021 study on Indonesian commercial banks (Handajani et al., 2024), bank diversification and external audit quality can reduce NPLs, which indicate credit risk. Effective bank risk management may minimize non-performing loans and raise profits.

The efficiency of a bank's operations can significantly impact cost savings, which in turn can improve the bank's overall financial performance. In the study, Mahmud et al. (2016) analyzed the influence of different bank-specific factors on the profitability of a sample of 15 commercial banks in Bangladesh from 2003 to 2013. The study assessed banks' size, operational costs, loans, and capital adequacy ratios. According to the study, low risk, efficient cost management, and proper bank size affect bank profitability. Ariyibi et al. (2020) examined how bank-specific factors affected Nigerian banks' financial performance from 2014 to 2018. According to their analysis, asset quality correlated negatively with ROA. Also noteworthy was the significant correlation between the loan-to-deposit ratio and capital adequacy. ROA, a precise financial metric, verified this correlation. Credit risk management and bank-specific factors significantly influence the financial performance of commercial banks in South Asia, according to a recent study by Siddique et al. (2021). Their research analysis shows that factors such as non-performing loans (NPL), cost efficiency, and liquidity ratios negatively impact financial performance. Nevertheless, the capital adequacy ratio (CAR) and average loan rate had a favorable impact on economic performance, as evidenced by the positive ROA and ROE. This suggests that Asian

authorities may build a stable economic climate by encouraging interest rates and developing a stringent monitoring system to eliminate NPLs. Commercial banks must maintain liquidity to survive in a competitive financial environment.

Agustini and Viverita (2011) found that bank-specific factors like profit lag, bank size, and bank capitalization affect profitability in Indonesia's banking system. External forces also affected the bank's financial development and concentration. Luu et al. (2020) observed that revenue diversification has benefited state-owned and foreign banks but hurt other non-government domestic banks. This study also shows that experienced banks benefit more from diversity. According to Moudud-Ul-Huq et al. (2020), bank size and revenue diversification affect financial performance, and more dependence on non-interest income increases returns. According to Zouari and Taktak (2014), family and foreign ownership improve Islamic banks' financial performance the most, followed by ultimate institutional ownership. Bank-specific characteristics significantly impact various aspects of a bank's financial performance. These include credit growth, net profit margin, provision for impairment losses, bank diversification, bank size, and ownership structure. The Central Bank's control system and the competence of bank management influence bank-specific factors, playing a crucial role in achieving positive financial performance. In consideration of the aforementioned arguments, the subsequent hypothesis is posited:

H_2: Bank-specific factors affect the bank's financial performance.

METHOD

This quantitative study explores how corporate governance ratings and bank characteristics affect Indonesian Stock Exchange-listed commercial banks' financial performance. The analysis was conducted on 35 Indonesian public banks listed on the Indonesia Stock Exchange from 2017 to 2021. The reason for using this observation period is because the obligation regarding corporate governance self-assessment was effectively implemented in commercial banks starting in 2017 based on the Financial Services Authority Circular Letter OJK Circular No. 13/POJK.03/2017 (OJK, 2017). Therefore, the use of observations during the year is relevant to provide an up-to-date picture of the regulatory implementation. The purposive sampling criteria are presented in Table 1.

No.	Sampling Criteria	Amount
1.	Public banking companies were listed on the Indonesia Stock Exchange during the observation period from 2017 to 2021.	47
2.	Banks do not provide annual corporate governance self-assessments for each observation period.	(5)
3.	Research data relating to the variables studied is incomplete and cannot be accessed through financial reports and annual reports published by banks.	(10)
4.	Number of sample banks	32
5.	Total number of observations (32 banks x 5 years)	160

Table 1. Sampling Method

This study utilizes audited financial reports and annual reports from go-public banking institutions from 2017 to 2021, as stated by the Indonesia Stock Exchange. This research uses data from banking companies that are consistently listed on the Indonesian Stock Exchange so that financial report data and annual reports related to the banking sector can be obtained via the website of the Indonesian Stock Exchange (https://idx.co.id). Audited financial statements are used because they produce financial statements that an independent auditor has audited by providing an opinion about the company's financial statements. Annual reports by banks that have public accountability as a communication medium that reports financial and non-financial activities to company stakeholders, including disclosing information related to the implementation of corporate governance, bank ownership, bank auditors, and other relevant data.

The exogenous variables in this research are corporate governance and bank-specific factors, while the bank-specific factors are endogenous variables. Corporate governance is essential for fostering transparency, accountability, responsibility, independence, and fairness when managing banks. According to the Financial Services Authority (OJK) Regulation No. 55/POJK.03/2016 (OJK, 2016b), which mandates that commercial banks carry out the implementation of corporate governance, this study ranks the findings of self-assessments on the subject of corporate governance implementation. A rating of one (1) indicates that the aggregate is extremely good, while a score of five (five) indicates that it is the lowest rating. The following is a classification of self-assessment composite scores according to Financial Services Authority Regulation No. 55/POJK.03/2016 (OJK, 2016b): 1 (Very Good), 2 (Good), 3 (Moderate), 4 (Less), and 5 (Poor). According to these regulations, the research in question evaluates corporate governance using each bank's annual GCG self-assessment ranking. This self-assessment was contained in the bank's annual report on corporate governance.

Bank-specific factors are among the various elements that distinguish one bank from another and have the potential to influence a bank's financial performance. Factors such as credit growth, loan loss provision, bank diversification, operational efficiency, bank size, external audit quality, and ownership are all considered in this study. It accomplishes this by referring to relevant publications (Ahmed et al., 2020; Ariyibi et al., 2020; Chen, 2006; Chiorazzo et al., 2008).

The bank's financial performance is a variable of interest in this study, which focuses on the situation. To evaluate the state of the health of banks, this study references Indonesian Financial Services Authority Regulation No. 4/POJK.03/2016 (OJK, 2016a). The study assesses banks' financial performance using the risk-based bank rating methodology. This methodology takes into account proxy indicators such as non-performing loans (NPL), loan deposit ratios (LDR), current account and savings account ratios (CASA), and return on assets (ROA). Measurements for each indicator of bank financial performance have been examined in various studies conducted by different researchers(Ahmed et al. (2021); (Handajani et al., 2024); (Kryeziu & Hoxha, 2021); (Okoye et al., 2020); (Abdallah & Bahloul, 2021); (Siddique et al., 2021); (Loan et al., 2024);(Jennifer et al., 2022)).

Table 2 provides a summary overview of the variables measured in this study, including both exogenous and endogenous latent variables, as well as the related indicators for each of these latent variables.

Variables	Indicators	Measurement	Reference Sources
Bank Financial Performance	Non-Performing Loan (NPL)	The percentage of substandard, doubtful, and bad loans to total loans disbursed	(Ahmed et al., 2021) (Handajani et al., 2024)
	Loan-to-Deposit Ratio (LDR)	The percentage of credit distributed to total funds deposited	(Kryeziu & Hoxha, 2021) (Okoye et al., 2020)
	Current Account and Saving Account Ratio (CASA)	The proportion of demand deposits and savings to the total amount of Third Party Funds	(Loan et al., 2024) (Jennifer et al., 2022)
	Return on Asset (ROA)	The percentage of net income to total asset	(Abdallah & Bahloul, 2021)
	Capital Adequacy Ratio (CAR)	Percentage bank's capital by its risk-weighted assets.	(Siddique et al., 2021)
Corporate Governance	Self-Assessment Corporate Governance	Rating of self-assessment GCG: 1 = Very Good; 2 = Good; 3 = Moderate; 4 = Less; and 5 = Poor	Financial Service Authority POJK No. 55/POJK.03/2016 (OJK, 2016b)
Bank-Specific Factors	Credit Growth	The ratio of loans-to-assets ratio	(Ahmed et al., 2020)
	Loan Loss Provision	The ratio of loan loss provisions provided	(Chen, 2006)
	Bank Diversification	The ratio of non-interest income to total income	(Chiorazzo et al., 2008) (Luu et al., 2020) (Moudud-Ul-Huq et al., 2020)
	Operational Efficiency	The ratio of non-interest expenses to total assets	(Chaity & Islam, 2022)
	Firm Size	Logarithm natural Total Asset	(Mahmud et al., 2016)
	Audit Quality	Dummy variable, 1 = If bank is audited PAFs Big Four, 0 = If bank is audited PAFs non-Big Four	(Handajani et al., 2024)
	Bank Ownership	Dummy variable 1 = State-owned banks 0 = Non-state-owned banks	(Zouari & Taktak, 2014)

Table 2. Measurement Variables

This study analyzed statistical data using descriptive statistics, measurement model test (outer model), and structural model test (inner model). The mean, standard deviation, maximum, and minimum values describe study variables.

This study employs a structural model in which the variables tested are unobservable (latent variables) and will be measured using manifest variables (indicators) to test the proposed hypothesis. The decision-making criteria for the outer model is a loading factor >0,5 for indicators, and the inner model uses a two-tailed test with a critical value of t-test>1,96. If the T value exceeds 1,96; the hypothesis is accepted, and conversely, if the T-test falls below 1,96; it will be rejected. The measurement of the outer model or structural model utilizes reflective indicators as manifest variables as outlined in the conceptual framework depicted in Figure 1. The construction of this conceptual framework model demonstrates the relationship between latent variables and observable variables (indicators). The structural equation model and measurement model were tested as follows:

$$CFP = \gamma_1 GCG + \gamma_2 BSF + \varepsilon_1 \quad (1)$$

$$CFP = \lambda_1.NPL + \lambda_2.LDR + \lambda_3.CASA + \lambda_4.ROA + \lambda_5.CAR + e_1 \quad (2)$$

$$GCG = \lambda_1.CG\ Rating + e_2 \quad (3)$$

$$BSF = \lambda_1.CG + \lambda_2.LLP + \lambda_3.BD + \lambda_4.BOE + \lambda_5.BS + \lambda_6.AQ + \lambda_7.BO + e_3 \quad (4)$$

where,

CFP	= Corporate Financial Performance
GCG	= Good Corporate Governance
BSF	= Bank-Specific Factors
NPL	= Non-Performing Loan
LDR	= Loan to Deposit Ratio
CASA	= Current Account Saving Account
ROA	= Return on Assets
CAR	= Capital Adequacy Ratio
CGRating	= Self Assessment of GCG
CG	= Credit Growth
LLP	= Loan Loss Provision
BD	= Bank Diversification
BOE	= Bank Operational Efficiency
BS	= Bank Size
AQ	= Audit Quality
BO	= Bank Ownership
γ (gamma)	= The coefficient of impact of exogenous variables on endogenous variables
λ (Lambda)	= Loading factor variable
ε_1	= Measurement model error on endogenous latent variables
$e_1, \ldots, e_3$	= Measurement model error on exogenous latent variables

Figure 1 below illustrates the conceptual framework of this study.

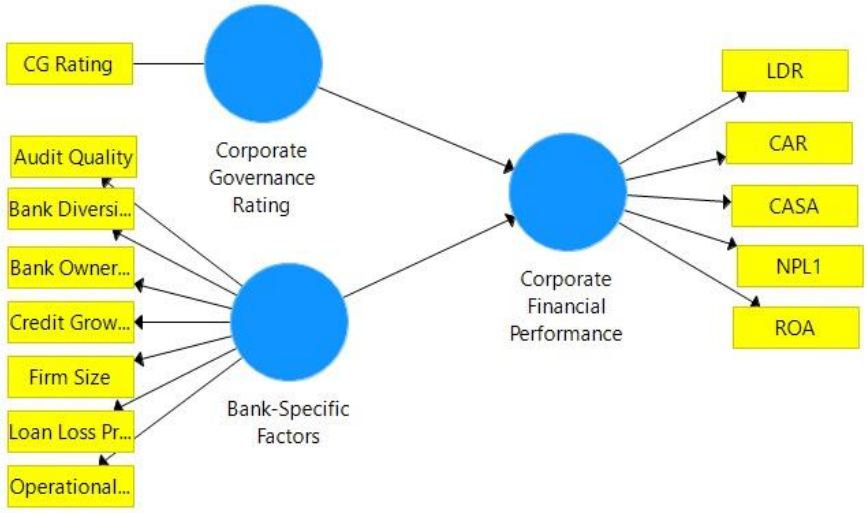

Figure 1. Conceptual Framework

RESULT AND DISCUSSION

Table 3 contains the statistical and descriptive data of this study. The valTo understand different ratios, like Non-Performing Loan (NPL), Loan Deposit Ratio (LDR), Current Account and Savings Account Ratio (CASA), Return on Assets (ROA), Capital Adequacy Ratio (CAR), Credit Growth (CG), Loan Loss Provision (LLP), Bank Diversification (BD), Bank Operational Efficiency (BOE), and Bank Size, look at the values of maximum, minimum, mean, and standard deviation. Frequency distribution tables in this study present data on the self-assessment of corporate governance, audit quality, and firm ownership.

Variables	Minimum	Maximum	Mean	Std. Deviation
Credit Growth	7,57	86,95	60,0194	13,21056
Loan Loss Provision	0,00	269,08	5,1179	28,77502
Bank Diversification	0,00	52,75	13,5832	9,65145
Operational Efficiency	-2,89	12,64	3,5178	2,16367
FirmSize	13,41	21,27	17,8084	1,81846
NPL	0,00	15,75	3,4153	2,15067
LDR	12,35	163,00	86,2186	21,66234
CASA	8,06	78,90	38,1665	18,85584
ROA	-15,89	4,45	0,6247	2,84662
CAR	10,52	169,92	26,6160	19,85682

Source: Secondary Data

Table 3. Statistic Descriptives

Credit growth has a mean value of 60,02%, indicating a fairly good growth in the number of loans each period. The maximum credit growth can reach 86,95%, but the minimum credit growth only gets 7,57%. In evaluating credit growth, the ideal credit distribution ratio for banks must be considered, namely in the range of 75%-80% to encourage bank economic growth while still maintaining bank health risks.

The loan loss provision averages 5,1179% and a maximum of 269,08%. Management inefficiency is reflected in the high value of the loan loss provision, which positively impacts the bank's actual losses. The bank's diversified portfolio demonstrates a mean value of 13,5832, with a maximum value of 52,75 and a minimum value of 0.00. It has been shown that including non-interest income in bank operations can effectively mitigate income volatility(Chiorazzo et al., 2008), as it is a valuable means of diversification (Chen, 2006). The operational efficiency exhibits a maximum value of 12,64 a mean value of 3,5178 and a minimum value of -2,89. The significant increase in operational cost efficiencies suggests a solid commitment to mitigating loan risk. On the other hand, lower operational costs can be a sign of the manager's skill in improving the bank's financial performance. To ensure efficiency in their day-to-day activities, banks must maintain an operational cost-to-bank operational income ratio of 60%, as per the Financial Services Authority's regulations.

The bank size variable indicates that the bank has a significant asset value primarily derived from a substantial number of loans. The variable's mean value is 17,8084, with a maximum value of 21,27 and a minimum value of 13,41. Non-Performing Loans (NPL) value ranges from a minimum of 0 to a maximum of 15,75, with an average value of 3,42. The NPL value serves as a measure of the credit management skills of bank managers. A lower NPL value suggests effective credit management, while a higher NPL value suggests a growing number of non-performing loans. Based on Bank Indonesia regulations, the average NPL value remains below 5%, presenting companies with the profit potential. The variable for Loan to Deposit Ratio (LDR) has an average value of 86,22%, with a maximum value of 163% and a minimum value of 12,35%. The loan-deposit ratio (LDR) is a measure that banks use to evaluate their liquidity. It entails comparing the total number of loans issued by a bank to the total number of deposits received within a specific timeframe. As the LDR ratio increases, the bank may face difficulties in meeting short-term obligations, such as customer withdrawals, as liquidity decreases. The study's findings reveal an LDR value of 86,22%, which aligns with the specified range of 78%–92% as outlined in Bank Indonesia Regulation (PBI) Number 15/7/PBI/2013.

The CASA ratio reveals an average value of 38,1665, which reflects the proportion of inexpensive (low-cost) funds in savings and current accounts out of the total third-party funds. The growing significance of CASA can lower the cost of funds and maintain the Net Interest Margin (NIM) stability. This is due to the reduced costs banks must bear to pay interest on deposits, enabling them to offer customers lower loan interest rates. Compared to the total deposits, the CASA ratio offers a clearer picture of the proportion of deposits held in current and savings accounts. A higher CASA ratio suggests a more favorable bank liquidity position as it reduces liquidity risk on the bank's interest margin. A solid understanding of the subject improves capital planning and bank management.

The ROA variable exhibits an average value of 0,6247%, with a maximum value of 4,45% and a minimum value of -15,89%. As the return on assets (ROA) increases, more net income can be generated from each unit of funds invested in total assets. An elevated return on assets indicates the company's ability to use its resources to generate profits

through operational activities. The sample banks achieved an average ROA value of 0,6247% and a maximum value of 4,45%. It is worth noting that these values are still below the minimum ROA limit of 5%. However, it is essential to consider that the standard ideal ROA value, as per Bank Indonesia regulation No.13/1/PBI/2011, is 1,5%, considering the specific characteristics of the banking industry. A higher ROA value suggests a more favorable utilization of bank assets. The Capital Adequacy Ratio (CAR) or minimum Capital Adequacy Ratio for commercial banks reflects the adequacy of existing capital to mitigate potential losses. The CAR has an average value of 26.62%, which exceeds the minimum requirement of 8% of risk-weighted assets (RWA), referring to Bank Indonesia's provisions under BI Regulation No.3/21/PBI/2001, which is considered prudent.

The frequency distribution for self-assessment corporate governance (CG Rating) variables, audit quality, and bank ownership are shown in Table 4.

According to Table 4,80% of sample banks have a CG self-assessment score with a rating of 2 (Good), while 11,3% have a very good rating (1), and the remaining 8,8% have a moderate CG rating (value of 3). The frequency distribution value for audit quality shows that 104 sample banks, or 65%, use auditors affiliated with Big Four (Big 4) Public Accounting Firms (PAFs), while the remaining 56 banks, or 35%, use non-Big 4 PAFs. PAF's Big 4 indicates a better audit program to increase the credibility of financial statements (The Indonesian Financial Services Authority, 2017). The frequency distribution of bank ownership is presented in Table 4, which shows that as many as 20 banks, or 12,5% are state-owned, while the remaining 140 banks, or 87,5%, are private (non-state-owned banks), whose capital source is not from the central government or regional government.

Variables	Categories	Frequency	Percentage
Corporate Governance Rating			
1	Very Good	18	11,3
2	Good	128	80,0
3	Moderate	14	8,8
4	Less	0	0,0
5	Poor	0	0,0
Total		160	100,0
Audit Quality			
0	Non Big Four PAFs	56	35,0
1	Big Four PAFs	104	65,0
Total		160	100,0
Bank Ownership			
0	Non-State-owned-Banks	140	87,5
1	State-owned-Banks	20	12,5
Total		160	100,0

Source: Secondary Data

Table 4. Frequency Distribution

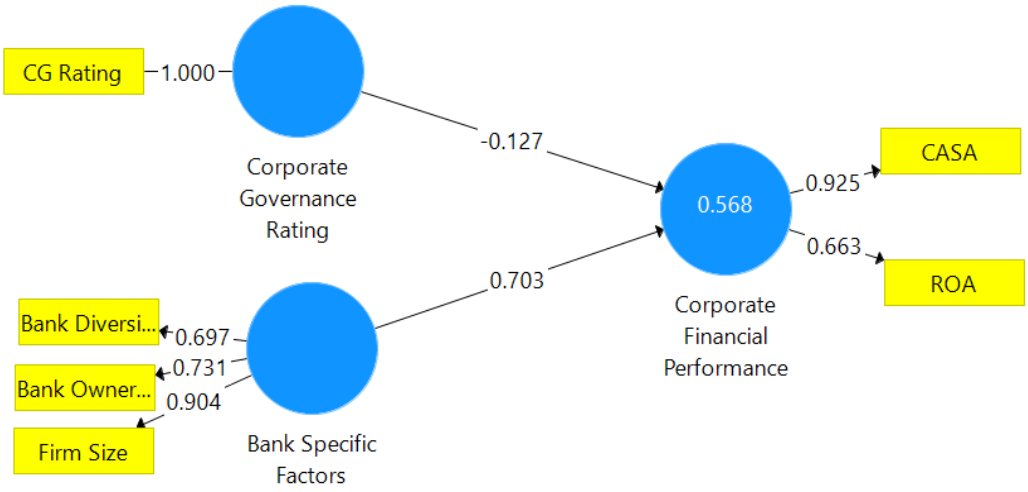

Figure 2. Measurement Model

Assessing the measurement model or outer model involves examining convergent validity and discriminant validity. The evaluation of convergent validity is based on the loading factor value of each indicator. When evaluating indicators, it is important to note that a correlation value above 0,7 is generally considered valid. However, it is also acceptable for the loading factor values to fall within the range of 0,4 to 0,6 (Hair et al., 2014). In the initial phase, the analysis of the outer model reveals that certain indicators have a loading factor below 0.6. These indicators pertain to exogenous variables such as audit quality, credit growth, loan loss provision, and operational efficiency. Similarly, endogenous variables like CAR, LDR, and NPL also exhibit a loading factor value lower than 0,6. The indicators that do not capture the essence of the latent variable (construct) are eliminated. Upon reevaluating the outer loading test, it is evident that all indicators possess an outer loading value exceeding 0,6 thereby confirming their convergent validity. Convergent validity is demonstrated when the indicators accurately reflect a single underlying variable, as indicated by the Average Variance Extracted (AVE). The conclusive outcomes of the measurement model recalculation test are exhibited in Figure 2.

Figure 2 shows the loading factor values for each latent variable indicator associated with bank-specific factors, namely bank diversification (0,697), bank ownership (0,731), and company size (0,904). The latent variable Bank Financial performance has a loading factor for each indicator ROA (0,663) and CASA (0,925), as well as a loading factor for CG rating (1,000) as an indicator of the latent variable Corporate Governance.

Testing discriminant validity can be done using Cronbach's alpha and composite reliability values. However, it is recommended to use a composite reliability value for measurement instead of Cronbach's alpha, as it yields a lower value. If the composite reliability value is greater than 0,70, it indicates that the construct is reliable. (Hair et al., 2014). The composite value of discriminant validity on each latent variable shows the consecutive values: bank-specific factor (0,824), corporate governance rating (0,782), and bank financial performance (1,000). Meanwhile, the average variance extracted (AVE) values show respective values for each latent variable: bank-specific factor (0,612), corporate governance rating (1,000), and bank financial performance (0,648). Thus, each variable has sufficient accuracy and consistency because its composite reliability value is above 0,70. Composite reliability tests show a measuring instrument's consistency. The tests show that each variable is accurate and consistent. A summary of the results of testing the measurement model (outer model) is presented in Table 5 below:

Variables	Convergent Validity	Discriminant validity	
	Loading Factors	Composite Reliability	AVE
Bank-specific factors		0,824	0,612
- Bank Diversification	0,697		
- Bank Ownership	0,731		
- Firm Size	0,904		
Corporate Governance Rating	1,000	1,000	1,000
Bank Financial Performance		0,782	0,648
- CASA	0,925		
- ROA	0,663		

Source: Secondary Data (2023)

Table 5. Measurement Model

After completing all the tests on the outer model, we can start testing the structural model (inner model). The ability of the structural model, also known as the inner model, to produce accurate predictions and to comprehend the connections between latent variables can be evaluated through the examination of the structural model. R^2 and f^2 calculations are critical in assessing the structural model. The R^2 value assesses the model's capacity to explain the impact of external factors on internal variables. When analyzing the effects of the exogenous variable on the endogenous variable, the determination coefficient is critical. The coefficient of determination predicts how the exogenous variable will impact the endogenous variable. Table 6 shows that the coefficient of determination of the endogenous variable financial performance is 0,568, or 56.8%, and the corrected R square is 0,563, or 56.3%. The impact size value (f2) measures model goodness and the contribution of exogenous variables to endogenous variables (Hair et al., 2014). The exogenous corporate governance rating variable contributes 0,033 whereas the bank-specific component contributes 0,028 indicating a minimal contribution. SRMR values below 0.10 indicate goodness of fit, while values above 0,15 indicate infeasibility. The SRMR value of 0,127 indicates feasibility. The normed fit index (NFI) is 0,627, which is below 0,90 indicating a decent model. Table 6 provides a summary of the outcomes of the structural model examination.

Exogenous Variables	Coefficients	t-Statistics	Probability
Corporate Governance Rating	-0,124	1,998	0,046**
Bank-Specific Factors	0,0705	16,797	0,000***
The Goodness of Fit Model			
R Square (R^2) = 0,568			
Adj. R Square = 0,563			
Effect Size (f^2) = 1,0280 ; 0,033			
SRMR = 0,127			
NFI = 0,627			

Notes: Statistical significance at α = 1%***; 5% **; 10%*

Table 6. Structural Model

Figure 3 presents the outcome of the structural model (inner model) test.

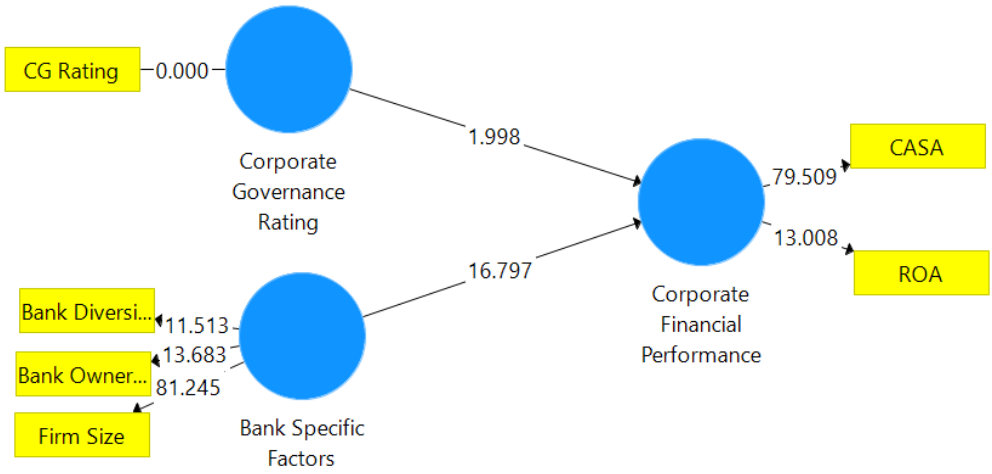

Figure 3. Structural Model

This study offers evidence supporting the initial hypothesis that suggests a connection between corporate governance and financial performance. The effect's significance is evident from the probability value of the corporate governance rating variable, which is 0,045 which is smaller than the alpha level of 5%. This suggests a statistically significant impact. A lower rating value indicates a higher GCG self-assessment rating, which is associated with improved financial performance. Conversely, a higher GCG self-assessment rating indicates a reduced influence on the bank's financial performance. The results of this study provide additional support for the second hypothesis, suggesting that certain factors unique to banks significantly contribute to their positive economic performance. The statistical analysis supports the study's findings, as it uncovers a bank-specific factor variable with a positive coefficient direction. The probability value of 0,000; which indicates statistical significance below 5%, reinforces the results. The research shows that various aspects of the bank, including diversification, ownership, and size, play a significant role in enhancing its financial performance, as indicated by the positive impact on metrics such as ROA and CASA.

The study's findings support prior research, indicating that the implementation of robust corporate governance practices has a favorable impact on the financial performance of banks, particularly on profitability. This study's findings align with previous research by (Abdallah & Bahloul, 2021; Ahmed et al., 2020; Basuony et al., 2014; Lai & Choi, 2014; Okoye et al., 2020). The findings are consistent with the descriptive statistical data on corporate governance ratings for the majority of the sample banks. The study included 128 banks, of which a significant 80% received good ratings, and 18 banks achieved very good ratings. Bank Indonesia issued a circular letter indicating that the GCG rating of commercial banks determines their level of good corporate governance (GCG) implementation. A lower GCG rating suggests a stronger implementation of GCG practices. It is clear that banks' governance practices, including their structure, processes, and outcomes, are indicative of sound and robust banking practices. Implementing healthy bank practices can positively influence the bank's financial performance, specifically its ROA and CASA, as indicated by an improving GCG rating. The average return on assets (ROA) is 0.6247%, and the maximum ROA is 4.45%. Typically, an optimal ROA value

hovers around 5%, but considering the unique characteristics of the financial industry, we recommend aiming for a range of 1.5%. This signifies a strong asset management position, which has the potential to enhance bank profitability. However, by increasing the proportion of low-cost funds (Current Account Saving Account/CASA), banks can effectively reduce their fund costs and increase their profitability. The statistical analysis findings reveal that the sample company's CASA funds total 38,1665 from third-party funds, with a maximum CASA ratio of 78,90%. Maintaining a low-cost funds ratio (CASA) between 30% and 70% is crucial for banks to ensure liquidity and efficient funding, thereby minimizing their reliance on high-cost customer deposits. However, the findings of this study challenge the conclusions reached by Benvenuto et al. (2021), Goel (2018), and Ovelar-Fernández et al. (2022), who argued that the adoption of corporate governance (CG) has a minimal impact on financial performance. Benvenuto et al. (2021) found that the CG index positively influences financial performance, especially in a highly homogeneous banking system. However, the banking sector, known for its diversity, has found that the CG index does not effectively promote the expansion of large banks.

The current study reinforces the findings of earlier studies (Artiningsih et al., 2011; Wahyudin & Solikhah, 2017) by affirming that the adoption of corporate governance practices in the Indonesian context has a positive impact on the financial performance of the banking sector. Given the circumstances, Bank Indonesia's involvement as a regulatory authority plays an important role in providing valuable insights into the adoption of corporate governance measures. The objective is to improve ratings and performance in the Indonesian banking industry. As additional evidence emerges, the study's findings support the conclusions of Wahyudin and Solikhah (2017) regarding the impact of corporate governance ratings on accounting-based financial performance indicators like ROE, ROA, and EPS. Nevertheless, in the near term, it does not have any immediate influence on market performance or company expansion. The results of this study indicate that improving the GCG rating can have a positive effect on the bank's financial performance, as shown by the enhancements in the CASA. A recently conducted study revealed a higher CASA ratio as a positive indicator of a bank's liquidity position (Bandyopadhyay, 2022). This is because a higher CASA ratio helps to mitigate liquidity risk on the bank's interest margin, resulting in more secure capital planning and bank management. In the end, this demonstrates strong bank governance. The study's findings indicate that it would be beneficial for regulators and capital market authorities to encourage the implementation of strong corporate governance practices to improve financial performance and increase firm value. We expect that the adoption of strong corporate governance practices in banking and financial institutions will create a positive work environment, leading to improved financial performance. Conversely, an ineffective implementation of a corporate governance system, demonstrating a lack of dedication to its principles, implies inadequate oversight and management within the organization, leading to adverse impacts on the bank's financial performance.

Upon careful examination of the second hypothesis, it becomes clear that there is a significant statistical correlation between certain factors related to the bank and the corporate financial performance. The bank-specific variable's probability value of 0 shows the effect's statistical significance. This score demonstrates that it is below the 5% alpha level. The positive coefficient indicates that various factors related to banks, such as their size, ownership, and diversification, positively impact their financial performance. The findings indicate that private banks, operating autonomously without government ownership and with minimal government intervention, have a substantial impact on

improving bank profitability. With their impressive resources and wide range of revenue streams, they can accomplish this. The study revealed that a significant portion of the banks in the sample (140 banks, or 87.5%) were privately owned or managed, as opposed to state-owned enterprises. The study's findings highlighted the positive impact of these prominent banks, known for their extensive operations and management of significant assets, on the bank's financial performance. The study revealed their significant contribution to the bank's return on assets (ROA) and deposits in current accounts and savings accounts (CASA). In contrast, there was a significant increase in bank diversification through non-interest income, with a substantial average rise of 13,5832% of total bank income. The highest level of diversification reached an impressive 52,75% suggesting that an increase in non-interest income has the potential to enhance the financial performance of banks.

This study confirms the findings of previous research by Mahmud et al. (2016) suggesting that specific bank factors like size and diversification management contribute to the profitability of commercial banks. Agustini and Viverita (2011) highlighted the significant impact of internal bank-specific factors like size and capitalization, as well as external bank-specific factors like ownership and concentration, on profitability, which aligns with the findings of this study. The study measured profitability using indicators such as ROA and ROE. The findings of this study further reinforce the conclusions drawn in prior studies (Brahmana et al., 2018; Luu et al., 2020; Zouari & Taktak, 2014). These studies suggest that when banks rely more on non-interest income, their financial returns improve, particularly in the case of state banks and foreign banks. This study confirms the findings of a previous study by Brahmana et al. (2018). The previous research also concluded that diversifying income sources, such as non-interest income, can enhance bank performance by mitigating risk through diversification.

Different metrics used to measure these factors lead to wide variations in results. As a result, it is critical to conduct more extensive testing to obtain dependable and uniform test results. The results suggest that to improve financial performance in banks, it is essential to have efficient bank management. The Central Bank and the Financial Services Authority can accomplish this by implementing regulatory oversight. These regulatory bodies play a critical role in ensuring the sound operation of banks.

This study's findings provide valuable insights into resource-based view theory (RBV theory) in the banking industry. The authors emphasize the significance of efficiently managing resources and managerial capabilities to improve banks' credit market share, service diversification, and operational efficiency. These factors ultimately play a crucial role in gaining a competitive edge in the financial industry and attaining optimal corporate financial performance. This study's findings provide additional support for the principles of agency theory by examining conflicts of interest among agents, shareholders, and regulators. The study emphasizes the importance of conducting self-assessments on corporate governance in heavily regulated financial institutions to effectively address these conflicts.

The findings of this study shed light on the importance of effective resource management and risk management in banks, along with the crucial role of good governance in promoting sustainable financial performance. The provisions set by Bank Indonesia regarding corporate governance self-assessments can establish effective practices that serve as governance mechanisms, motivating banks to thrive and achieve economic success in a highly competitive financial industry. The results of this study could enhance banking

management practices by promoting the adoption of effective corporate governance measures. This, in turn, would foster greater transparency, accountability, responsibility, independence, and fairness within financial institutions.

Regarding policy implications, the study's findings suggest that tighter regulations, monitoring, restrictions, robust supervision, and more outstanding capital and new reforms will help improve bank management efficiency and attain optimal bank performance. The provisions of the Financial Services Authority through OJK Regulation Number 55/POJK.03/2016 (OJK, 2016b) and Bank Indonesia regulation number 13/1/PBI/2011 (BI, 2011) related to assessing the soundness of a bank will encourage bank compliance in responding to it by implementing good governance in the banking sector to encourage compliance in the management of banking financial institutions towards the sector sound banking.

CONCLUSION

This study provides empirical findings on the impact of corporate governance and bank-specific characteristics on the financial performance of banks listed on the Indonesian Stock Exchange from 2017 to 2021. The study's findings highlight the crucial role of strong corporate governance practices in driving the financial performance of banks. Ratings of corporate governance self-assessment and bank-specific factors measure this impact. The findings indicate that a more thorough assessment of corporate governance can yield favorable outcomes for the bank's financial performance. This is evident through an increased return on assets and a more significant proportion of low-cost funds (CASA ratio). Additional investigation reveals that a range of factors unique to banks, such as their ownership structure, size, and diversification, play a crucial role in shaping the financial performance of these institutions. This study highlights the importance of adhering to regulatory requirements, such as incorporating self-assessment mechanisms for corporate governance, to foster strong banking practices. The effective allocation and utilization of resources by bank management to achieve financial performance requires the implementation of robust corporate governance practices that ensure compliance with the bank's evaluation of stability. Sound management strategies in the banking sector are crucial for fostering a culture of solid banking practices and encouraging financial institutions to adopt effective governance practices.

This study recognizes certain limitations in the complexity of the proxies utilized to measure indicators connected to bank governance and the indicators employed to evaluate bank financial performance and bank-specific factors. This study investigates how corporate governance is implemented through self-assessment in the Indonesian environment, which is an emerging market. For future research, it may be worth considering examining content analysis disclosure guidelines or other measurement proxies tailored to the banking sector in various countries. This approach has the potential to offer valuable insights into the practices of corporate governance. Prior research has employed different metrics to assess banks' distinct attributes and financial performance. However, the study has yielded mixed results regarding the impact of these factors on a bank's financial performance. To improve the relevance of future studies, we suggest expanding the sample size and implementing different measures to evaluate banks' financial performance and market performance. This will enable a more thorough analysis of how the quality of bank governance and bank characteristics impact investor decision-making.

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