CHAPTER 1

INTRODUCTION

1.1 Background

The banking industry has hold important role for economic development as a financial intermediary or intermediaries the excess funds to the parties that need the funds in accordance with the legislation of the Republic of Indonesia No. 10 of 1998 about banking that the bank is a business entity that gathers funds from society in the form of savings and channel it to the community in the form of credit and other forms or in order to improve the people's livelihood.

In analyzing the financial position and assess the progress and potential in the future, the main factors that generally get attention by analysts is: (1) liquidity, which shows the company's ability to meet its financial obligations must soon filled in the short term or at maturity. 2) the solvency, the company's ability to meet all its obligations, whether short term or long term, if the company is liquidated,and (3) profitability, which demonstrates the company's ability to generate profits in the period. (Sianturi, 2012)

Bank health level is assessing a condition of bank financial statements on a specific time period and in accordance with Bank Indonesia standards (Riyadi, 2004: 149). To assess the Bank health Level can be measured by various methods. Health assessment will affect the ability of the bank and customer loyalty towards the bank in question. One of the tools to measure the health of the banks is the analysis of the 5 aspects, namely Capital, Assets, Management, Earning, Liquidity. These aspects are then assessed using financial ratios so that it can assess the financial condition of the banking companies (Kasmir, 2008: 273). Aspect capital can be assessed through a Capital Adequacy Ratio (CAR), the aspects of assets is assessed with the Non Performing Loan (NPL), earning aspect includes the Return On

Asset (ROA), Net Interest Margin (NIM), and BOPO, whereas liquidity aspect include Loan to Deposit Ratio (LDR).

Profitability is the most important indicator to measure the performance of a bank. Return On Assets (ROA) focusing the company's ability to obtain earning activities in company operations by utilizing its own assets. So in this study ROA is used as performance measures of banking. The main purpose of the bank is achieving operational levels of maximum profitability. ROA is important for the bank because of the ROA is used to measure the effectiveness of the company in generating profits by making use of assets. The profitability of the bank's ability to generate/obtain it effectively and efficiently. Profitability used is ROA as it can take into account the ability of the bank's management in managing its own assets to generate income. The larger the ROA a bank, the greater the profit level achieved is the bank and the better the bank's position also in terms of the use of the asset (Dendawijaya, 2009: 118).

The existence of state-owned banks in Indonesia, local governments, the private sector can be categorized national domestic and foreign-owned and joint venture banks is quite interesting to highlight. It is with regard to its existence that much come into contact with the real sector activities. So the conditions are felt by the banking sector greatly affect other sectors of the economy.The entry of joint venture banks to encourage domestic banks to improve efficiency and increase the diversity of this nation and the quality of financial services in order to maintain market share. Further, the entry of joint venture banks associated with the costs, profit margins and interest as well as on a higher economic development (Astohar2009)

For an international-scale banking requires efforts to serve clients worldwide, so it does not cover the possibility of the bank opened branches in foreign countries or the existence of the bank so that foreign banks abroad, However a minimal capitalization for banks or by reason of the bank's efficiency is working with domestic banks setting up new overseas bank (Joint venture bank).The presence of Joint venture banks give impact for local (private, Government or local government). Many banks compete to create profit as an indicator of company performance (Gelos 2006)

The entry of joint venture banks can improve the quality and availability of financial services on the domestic market with increased competition, opening opportunities for better application skills and modern banking technology, encourage the development of bank supervision and the legal framework, and improves a country's access to international capital markets.

Examining the performance of joint venture banks, what determines the success and how the performance of different domestic banks with the joint venture bank’s. Structure and the different characteristics of joint venture banks and domestic banks, and different effects of external factors on the banks, on the other hand can lead to performance differences between the two categories is an interesting thing.

Empirical analysis of the performance of domestic banks and joint venture banks will illustrate if the implementation of banks in different ways as well as the reason for the difference. This helps clarify how the performance of joint venture banks operating in Indonesia and also look at the ratio a bank's financial statements of joint venture banks. Bank Indonesia (BI) noted, foreign banks and joint venture banks offer interest rates on working capital loans (KMK) is much more interesting than the commercial banks. According to statistics rupiah loan interest rates, foreign and joint venture banks offer interest rates below 10%. "Mortgage interest rates rupiah foreign and joint venture banks for working capital last data recorded 9.34%. During the year 2011 the foreign banks and joint venture banks on average provide working capital loans at 9% position, " from this statement i want to see, how performance from joint venture bank to increase bank profitability.

There are some government policy in banking Government policies in the areas of banking, among others is a package of deregulation. The Government's policy of deregulation of banking is viewed from one side is indeed capable of producing progress but also had a negative impact that caused the closure of several banks.This situation proves that banking Indonesia does not have a strong foundation so that this problem occurred on liquidity and solvency.

The liquidity ratio is the ratio that is required in analyzing the financial statements of the company. because the ratio of Liquidity is the ratio that indicates the company's ability to meet short-term obligations that must be met (Ningsih, 2011). The issue raises depositors distrust both within and outside the country to invest, what happens is a result of capital flight out of the country by investors. Financial statements of banks is very poor with a negative net income and capital adequacy Capital Adequacy Ratio (CAR) are not met. The implication of these provisions is the banks have restrictions on credit expansion in the show by the Loan to Deposit Ratio (LDR). Restriction to credit expansion will lead to the growth of the bank, (Pasaribu,2011)

In conducting the assessment of Capital adequacy, the Bank should also associate the capital requirement with the Bank's risk profile. The higher the Risk, the bigger the Bank's capital should be provided to anticipate those risks. The level of capital adequacy is represented by Capital Adequacy Ratio. The high capital adequacy and adequately will increase the volume of banking credit. In other word Capital Adequacy ratio (CAR) has a positive effect on bank’s profitability. It is similar with research conducted by Heriyanto (2009)which found Capital adequacy Ratio have a positive and significant influence on bank’s profitability in term of Return on Asset (ROA) Astohar (2009) And Gelos (2006) also found Capital Adequacy Ratio a positive effect on Return on Asset. Besides that, Sabir (2012) found Capital Adequacy Ratio have no effect on bank’s profitability.

LDR revealed how far the bank's ability to repay withdrawals made by relying on the depositor's customer credit given as a source of liquidity.The higher this ratio, the lower is the ability of the concerned bank liquidity. A high ratio indicates that a bank lends the entire funds (loan-up) or relatively illiquid. Otherwise a low ratio indicates that banks liquid with overcapacity funds ready for lent.The result of research conducted by Anggita (2011) and Astohar (2009) shown Loan to Deposit ratio (LDR) has significant and positive effect on Return on Asset (ROA) meanwhile Sumarni (2012) and Sabir (2012) found that Loan to Deposit ratio (LDR) has negative and significance effect on Return on Asset(ROA).

From the previous research above, there is has a different result of the research. Because of that, an author interested to review the hypothesis and obtain an evidence about influence of Capital Adequacy Ratio (CAR) and Loan to Deposit Ratio (LDR) on bank's profitability in the form of Return on Asset (ROA). The author would like to do a research entitled**"The Influence Of Liquidity Ratio and Capital Adequacy Ratio to Bank's Profitability on Joint venture Banks in Indonesia in period 2010-2012.**

1.2 Problem Definition

Based on the research background, then the problem can be determined in this study, namely:

1. How does the Capital Adequacy Ratio (CAR) influence on profitability measured by Return on Assets at Joint Venture Banks?
2. How does the loan to deposit ratio (LDR) influence on profitability measured by Return on Assets at Joint Venture Banks?
3. How does the of Capital Adequacy Ratio (CAR) and loan to deposit ratio (LDR) simultaneously influence on profitability measured by Return on Asset?.

1.3 Research Objectives

The objectives of this study are as follows:

1. To obtain empirical evidence about the influence of Capital Adequacy Ratio (CAR) on profitability.
2. To obtain empirical evidence about the influence of Loan to Deposit Ratio (LDR) on profitability.
3. To obtain empirical evidence about the influence Capital Adequacy Ratio (CAR), Loan to Deposit Ratio (LDR) simultaneously on profitability.

1.4 Research Benefit

Practical usefulness of this study are expected to provide input or information that is useful for:

1. Author

   This study is very useful for the writer as it can add to and expand the knowledge and understanding of the author of the analysis of financial ratios and their effects on the financial performance of the company, especially a company that is engaged in banking.

2. Academic

   This study is expected to provide useful input as well as additional reference material for students majoring in either accounting or other interested parties, to be used in the problem or the results associated with financial ratios, and company's financial performance.

3. Other Parties

This research is expected to be useful for others who want to know how the financial performance analysis techniques using the tools in the form of certain financial ratios that can be useful as a material consideration in deciding the appropriate policy for the company.

1.5 Writing Systematic

The writing systematic of this study is divided into five chapters and each chapter divided into some subchapter. The first chapter are describes about the research backgrounds, problem definitions, research objectives, research benefits, and writing systematic.

The second chapter is literature review, theoretical framework and hypothesis that discuss about the theoretical analysis of this study that gathered from some sources, such as books, journals, internet, and previous research and discuss about hypothesis development.

The third chapter discusses the research methodology used in the preparation of this study, type of research, population and sampling, variable definition and measurement, types of data, data collection method, data analysis method, classical basic assumption and hypothesis testing which used to analyze the data and any information needed.

Chapter fourth describes the result of research based on the data and information gathered related with problems definitions.

The last chapter is conclusions , this chapter presents the conclusions which consist of the entire conclusion that have been taken and also consist of suggestion from the author as a result form the problem that hopefully will be useful for certain of people.