BOARD EFFECTIVENESS AND FIRM PERFORMANCE, THE CASE OF ISLAMIC BANKS

THESIS

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ABSTRACT

The measuring of previous of firm's performances is one of the best ways for all parties that are interesting to the firm to predict its performance. The case of this study is Board Effectiveness and ownership structure, in point of view corporate governance, of Islamic Banks in Indonesia. This research use book value approach to measure firm's performance that is influenced by board composition, where board composition of the firms consist of number of board of commissioners, independent commissioners, and differences between majority and non majority shareholders. Firm's performance is represented by Return on Asset (ROA), Return on Equity (ROE), BOPO, and Net Interest margin (NIM).

This research is designed as descriptive analysis for sample 2004 – 2007. The analysis output validity tested by using coefficient of correlation and ANOVA model. The result of the analysis: 1) The number of board commissioners have significant influence to the Islamic Bank's performance toward ROA, ROE and BOPO, except in NIM indicators 2) Proportion of Independent Commissioners have significant influence towards ROA, ROE, BOPO, except NIM indicators. 3) There is significant differences between majority shareholders toward non-majority shareholders towards ROA, ROE, except in BOPO and NIM indicators

Keywords: Corporate Governance, board effectiveness, independent commissioners, board size, Islamic Banking

CHAPTER I

INTRODUCTION

1.1 Background

Corporate governance is company key to success to growth and become profitable in long term period and sustain in global competitive global. The financial crisis of 1997-1998 that swept through most of East Asia has highlighted the need of financial and governance reforms in the region. The cause of economic crisis that have happened in Asia and South America believe of failed in applying Corporate (Daniri, 2006). And it gives us description that good corporate governance is useful for stakeholders and positive effect for wide scale of national economic growth.

Since Indonesia have been fall in crisis and known that time waste in repairing process caused by weaknesses of corporate governance applied by company, so government and investor start to give significant focus in corporate governance practices. In the case of Indonesia, capital markets are less developed and there is lack of information available to the public on company's performance (Patrick 2001; Lukviarman 2004). Therefore, there are obstacles in the market for corporate control mechanism to effectively work in Indonesia. Hence it can be argue that the governance implementation process within this country heavily lay on the internal governance mechanisms (Lukviarman 2004).

Corporate governance has known globally, especially in last 10 years. Corporate governance as system and mechanism to operate the company, purpose to enhance the stakeholders' value and others side that becomes important side with company such as creditor, supplier, consumer, employee, government, and common people. The four standard principles to apply the good corporate governance in company are *transparency, accountability, fairness and responsibility.*

Two types in applying corporate governance are Market Based corporate governance and Relationship Based corporate governance. The external mechanisms which commonly called market for corporate control rely on the effectiveness of the market in providing discipline over a company and the legal regulatory system (Lukviarman 2004) while the internal mechanisms include managerial incentives schemes, board of directors monitoring role and accountability reinforced by credible external auditing procedures (Patrick 2001).

The dominant view of corporate governance hinges on the issue of separation of ownership and control within the firm, which is modeled by "the agency theory" (Keasey, Thompson & Wright 1997; Demirag 1998). Agency theory is a perspective which clearly describe the potential conflicts arises by the separation of ownership and control, known as the agency problem, as argued by Jensen and Meckling (1976). Problem arises when the agent (e.g. borrower) have had different interest with the principal (provider of finance e.g. lender). To avoid such problems the companies have to implement the concept of control that will further develop as good corporate mechanism of control.

CHAPTER V
CONCLUSION

The purpose of this research is to get the statistical data that show the influence of board composition toward the financial performance as a base to evaluate the company performance as a whole. According to the data analysis and discussion that have been explained in the previous chapter, the conclusion, implementation, and constraints of this research will be explain as follow:

5.1 Conclusion

1. In this research, the significance influence between total amounts of Board of Commissioners and proportion of Independent Commissioners in Board of Commissioners toward the company's financial performance analyzed in single regression analysis. Single model used to analyze the significant influence of total amounts of Board of Commissioners and proportion of Independent Commissioners in Board of Commissioners toward the financial performance. T-test analysis used to analyze the influence and differences of toward the financial performance.
2. According to the result of data analysis, total amounts of Board of Commissioners performance toward ROA (Return on Asset), ROE (Return of Equity), BOPO and NIM as a measure of company book value According to the hypothesis testing can be conclude that:

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