The Effect Of Corporate Governance And Corporate Strategy On Family Firm Performance In Indonesia

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ABSTRACT

This paper analyzes the influence of corporate governance and corporate strategy on the performance of family owned or controlled firms listed on the Indonesia Stock Exchange. The Corporate Governance proxy is Family Ownership and Independent Commissioner, and Corporate Strategy proxies are Diversification and Compensation Strategy of Directors. This study uses a sample of 70 companies that are family owned or controlled companies listed on the Indonesia Stock Exchange (IDX) from 2014 to 2018. Data analysis was performed using multiple linear regression methods. The results of this study indicate that family ownership has a significant negative effect on company performance (ROE). While diversification and compensation strategy of directors have no effect, firm performance is measured by ROE.

Keywords: Family Ownership; Business Strategy; Corporate Performance

INTRODUCTION

Good Corporate Governance (GCG) is a concept that concerns the company's structure, division of tasks, division of authority, and division of responsibilities of each element of the company. The principles of Good Corporate Governance include Transparency, Accountability, Responsibility and Fairness. Good Corporate Governance (GCG) is a system that regulates and controls companies that create value added for all stakeholders, both primary stakeholder investors such as employees and managers, suppliers, business partners and the community and secondary stakeholders such as the government, institutions, businesses, social groups, academics and competitors.

Agency theory argues that family management is useful in achieving family goals and will later influence decisions which then have an impact on company performance (Anderson & Reeb, 2003). Families that manage companies tend to look for additional skills to improve the well-being of themselves and the company and increase the family's reputation. Allouche, Amann, Jaussaud, and Kurashina (2008) found that family firms in Japan showed better performance based on 1998-2003 data. Saito (2008) confirms these results. However, Cucculelli and Micucci (2008) found no indication of performance superiority in family companies in Italy. Sciascia and Mazzola (2008) found a negative relationship between family interference in management and company performance in 620 private companies in Italy. Miralles and Miralles (2014) found a negative impact between family management and company financial performance. In Portugal and Spain, the impact of family management on company performance can be positive or negative. Anderson, Reeb, Upadhyay and Zhao (2011) argue that this happens because families do not always act in the best interests of the company. Research by Leung, Richardson and Jaggi (2014) show that the appointment of an independent director in the directors of a family company does not affect the company's performance. Kim and Gao (2013) found that the long-term goals of the company bridge the relationship between family management and company performance.

Fernandes (2008) study related to compensation of directors and company performance and showed no relationship between the two. However, Duffhues and Kabir (2008) found a negative relationship between compensation for the board of directors and company performance. Kato and Kubo (2006) analyzed CEO compensation for companies in

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Japan and found a positive pay-performance relationship. In the Philippines, Unite, Sullivan, Brookman, Majadillas, and Taningco (2008) found a positive relationship between executive compensation and company performance. Theeravanich (2013) found a positive relationship between directors' compensation and the performance of family companies and higher compensation payments to family companies in Thailand.

LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

The existence of family business groups in Indonesia usually starts from companies that are purely owned by the family. The development of the company's business follows a predictable pattern according to their business development. The development of the company has the characteristic of concentration of family ownership that is maintained even though it eventually becomes a public company through selling shares in the capital market. Family ownership in the corporate governance system is something that needs to be considered because businesses in Indonesia are more owned by families, Harjito and Martono (2014). Lukviarman (2016) explains that family-based business is based on two main things, namely, to protect family interests and distrust of family members of other parties that are outside the family. Cucuellli and Micucci (2008) explained that family share ownership has a negative impact on financial performance. Anderson and Reeb (2003) explain that family ownership has a negative impact on financial performance because the legal protection provided to investors in ownership structures tends to be weak. Based on the description, the first hypothesis in this study is:

H1: There is a negative relationship between family ownership and company financial performance.

An independent commissioner is a party that ensures the existence of Good Corporate Governance in the company by providing input and supervision to the Board of Directors for the company's benefit. Fama and Jensen (1983) state that non-executive directors (independent commissioners) can act as mediators in disputes between internal managers and oversee management policies and provide management advice. Independent commissioners are members of the board of commissioners from outside the company who are not employees and do not have financial, management, or share ownership relationships. Research conducted by Manik (2011) shows that Independent Commissioners have a positive effect on company performance. Trisnantari (2008) showed that Independent Commissioner had a positive effect on financial performance. Based on these descriptions, the second hypothesis in this study is

H2: There is a positive influence of the Independent Commissioners on a company's performance.

Compensation is an important factor that influences why so many people work in a particular organization and not in other organizations in this case the company must be comprehensive in providing compensation to employees to maintain and provide appropriate compensation for them. There are two types of compensation given to employees, intrinsic compensation and extrinsic compensation. Intrinsic compensation is compensation in the form of praise given to employees with the impact obtained is a psychological impact while extrinsic can be in the form of things that are direct and indirect. Direct compensation can be exemplified as a basic salary while indirect compensation such as benefits provided to employees. According to Conyon (2006), the amount of compensation given for high performance of the company in that period, if the company's financial performance falls, then the compensation of directors will decline, and vice versa. However, if the directors get compensation incentives that are too large compared to the industry average and are not in accordance with the complexity of their duties and responsibilities, the excess compensation may affect the company's performance, Chen (2013). Canarella & Nourayi (2008) found a non-linear relationship between compensation and company performance. Based on the description, the third hypothesis in this study is:

H3: There is a positive relationship between Compensation of Directors and Company Performance.

Diversification strategy is defined as a strategic alliance of the core competencies of various skills and technologies owned by the company so that resources can be implemented in business segments that exist in the company. Diversification strategy based on competencies, resources and core businesses owned by the company is the implementation of a diversified relationship (related diversification). Chatterjee and Wernerfelt (1991) found that diversification strategies have a positive influence on firm performance so that the fourth hypothesis of this study is:

H4: There is a positive relationship between Diversification Strategy and company performance.

RESEARCH METHOD

The population in this study are family companies in Indonesia with a sample of family companies listed on the Indonesia Stock Exchange (IDX) with a total of 112 companies during the period 2014-2018 (5 years) using a purposive sampling method determined based on certain criteria, obtained 70 companies as a sample of companies listed on the Indonesia Stock Exchange during the study period. The dependent variable in this study is performance (ROE). While the independent variables are: First, family ownership, which is measured using a large percentage of family ownership of total ownership in the company. Second, the directors' compensation is taken using the total compensation given to the Board of Directors. Third is an independent commissioner, which is measured using an indicator of the total number of independent commissioners from outside the company of all sizes of the company's board of commissioners. Fourth is the diversification strategy shown by using the number of business units or subsidiaries owned by the company obtained from the company's financial statements.

RESULTS AND DISCUSSION

Descriptive Statistics

Descriptive statistics of 70 sample companies are in Table 1.

Table 1. Descriptive Statistics

No	Variable	Mean	Minimum	Maximum
1	Return on Equity	13.3 %	1%	31.94%
2	Family ownership	42.22%	18%	84.11%
3	Independent commisionary	32.92%	16.67%	66.67%
4	Diversification	4	1	8
5	Director compensation (million Rp)	Rp3,422	Rp1,289	7,130

The regression results of Family Ownership, Independent Commissioners, Diversification, and Directors' Compensation for Financial Performance (ROE) are in Table 2.

Table 2. T test results for Linear Regression Dependent Variable ROE

Variable	Beta (β)	t-stat	*P- Value*
Constant	0.041	0.245	0.871
Family ownership	-0.037	-2.875	0.028
Independent commissioner	0.211	2.796	0.003
Diversification	0.011	1.327	0.321
Compensation of directors	0.004	0.146	0.763

Sumber: Data diolah, 2019.

Discussion

Based on the first hypothesis test, that family ownership of family company negatively influences financial performance of family owned or controlled companies in Indonesia, has a significant negative influence ROE. These results are consistent with research conducted by Cucuelli and Micuci (2008) that family ownership has a negative impact on financial performance and in accordance with the results of research conducted by Anderson and Reeb (2003) states that family ownership has a negative impact on family businesses in Indonesia.

The second hypothesis test results show that the independent commissioner has a positive and significant effect on the company's financial performance using (ROE). The results of testing the third hypothesis indicate that the diversification strategy has no effect on financial performance (ROE). This empirical result is consistent with Setyawan (2013) that diversification does not affect the company's performance (ROE). The fourth hypothesis test results indicate that there is no effect of Compensation on the Performance of Family Companies in Indonesia, Return

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on Equity (ROE). This is in consistent with Theeravanich (2013), that Directors' Compensation has no effect on company performance. This compensation strategy is one of the control mechanisms used to attract the workers from outside and to regulate the rate of management turnover in the company.

CONCLUSION

The results of this study show that family ownership negatively influences performance (ROE) of family-owned business listed on the stock exchange in Indonesia. Independent commissioners positively and significantly influence the company's performance of ROE. Diversification strategy and compensation of directors do not significantly influence ROE.

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