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Effect of Risk, Capital, Good Corporate Governance, Efficiency on Financial Performance at Islamic Banks in Indonesia

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Abstract: *The purpose of this study is to determine the factors that influence risk management, capital, GCG, and efficiency on the financial performance of Islamic commercial banks in Indonesia. The population in this study were Islamic commercial banks in Indonesia and selected by purposive sampling and selected 10 Islamic commercial banks. The period of this research is from 2014 to 2019. The independent variables are risk, capital, GCG and efficiency, while the independent variable is financial performance. The process of collecting data is through downloading the annual report of each bank. Data analysis was carried out by descriptive analysis and statistical analysis, using Smart-PLS software. The results of the study are that risk has a significant effect on capital in Islamic commercial banks in Indonesia; 2. Risk has no significant effect on efficiency in Islamic commercial banks in Indonesia; 3. Risk has a significant effect on GCG in Islamic commercial banks in Indonesia; 4. Risk has no significant effect on the financial performance of Islamic commercial banks in Indonesia. 5. Capital has no significant effect on the efficiency of Islamic commercial banks in Indonesia; 6. Capital has a significant effect on the financial performance of Islamic commercial banks in Indonesia; 7. GCG has a significant effect on the efficiency of Islamic commercial banks in Indonesia; 8. GCG has no significant effect on the financial performance of Islamic commercial banks in Indonesia; 9. Efficiency has a significant effect on the financial performance of Islamic commercial banks in Indonesia.*

Keywords: *Risk, Capital, GCG, Eficiency and Financial Performance*.

I. Introduction

In connection with the increase in Islamic banks operating in Indonesia, Islamic banks already operating in Indonesia are required to be able to manage their operations efficiently. Sharia banks that are efficient in their operations are expected to be able to defend themselves in the competition of the banking industry, both with fellow Islamic commercial banks and conventional banks. The reason for using the object of research on Islamic commercial banks is because until now the market share of Islamic commercial banks is still only around 5%, while their performance is quite good.

The management of banking operations must be able to manage the appropriate use of the sources of funds that have been collected and their distribution and accountability. Regarding efficiency, what generally gets the attention of banks is how banks can manage operational costs and operating income and involve assets in the process. These operational activities need a process of identification, measurement, analysis, and communication of financial information used by management for planning, controlling, evaluating bank operations.

The purpose of this study is directed to analyze the factors of risk management, Capital, Corporate Governance (CG), the level of efficiency of Islamic banking that affect the financial performance of Islamic commercial banks in Indonesia.

Problem Formulation, Based on the description of the background of the problem, the formulation of the situation in this study is :

1. Risk affect the Capital of Islamic Commercial Banks in Indonesia
2. Risk affect the efficiency of Islamic Commercial Banks in Indonesia
3. Risk affect Good Corporate Governance in Islamic Commercial Banks in Indonesia
4. Risk affect the financial performance of Islamic Commercial Banks in Indonesia
5. Capital affect the efficiency of Islamic Commercial Banks in Indonesia

6. Capital affect the Financial Performance of Islamic Commercial Banks in Indonesia
7. Good Corporate Governance affect the efficiency of Islamic Commercial Banks in Indonesia
8. Good Corporate Governance affect the financial performance of Islamic Commercial Banks in Indonesia
9. Efficiency affect the financial performance of Islamic Commercial Banks in Indonesia

II. Literature Review

The factors affecting banks' performance have been empirically examined by many authors.Eric et al, 2016, one of the objective oh the study to ascertain whether there is a significant relationship between risk management and bank performance. The finding that risk management is positively related to bank performance of GSE listed banks when tehe letter is measured from ROE perspective.

Sutrisno, 2016, conducted research on Islamic Banks in Indonesia, the result showed the significant effect of FDR, CAR, OEOI and size on the financial performance of Islamic Banking in contrast to the RR and NPF that had no significant effect on the performance of Islamic Banking.

Benyamin, 2015,the objective of this study was to assess the effect of risk management on the financial performance of Islamic bank in Kenya.The finding of the study that credit risk, insolvent risk, interest rate sensitivity negatively affect the financial performance and that there was a positive relationship between capital adequace, size of the banks, operational efficiency and financial performance

Zulkifli N. A. et al, 2015, in his research with the aim of examining the relationship between liquidity risk and performance of conventional banks and Islamic banks. The results of his research show that the most significant factor is capitalization, and capitalization also has a strong relationship on performance by using the parsimonious model.

Georgios E. C., Claudia G and Alexia V. 2011, Research with the aim of investigating the dynamics between financial frictions, efficiency and risk for the eurozone's commercial banks. The finding is that the validity of financial frictions and consistent with efficiency-lending quality.

Abdul Mongid and Izah M.T. 2010, conducted research on Rural Banks in Indonesia, with the aim of estimating the technique and efficiency scale using a non-parametric-DEA approach. The results of the study stated that the level of technical efficiency is lower than the level of efficiency scale, this indicates inefficient.

Altunbas Y. et al. 2007, conducted a research entitled: Examining the Relationships between Capital, Risk and Efficiency in European Banking. The purpose of this study is to analyze the relationship between Capital, Risk and Efficiency, for a large sample of banks in Europe from 1992-2000. The results of the study, that companies that have strong finances will have an effect on reducing bank risk and also the level of capital.

Based on theoretical studies as well as empiric studies such as the explanation in the previous chapter, as reference material/sources, reference related to the research carried out, the framework for the thought process of this research can be made as follows:

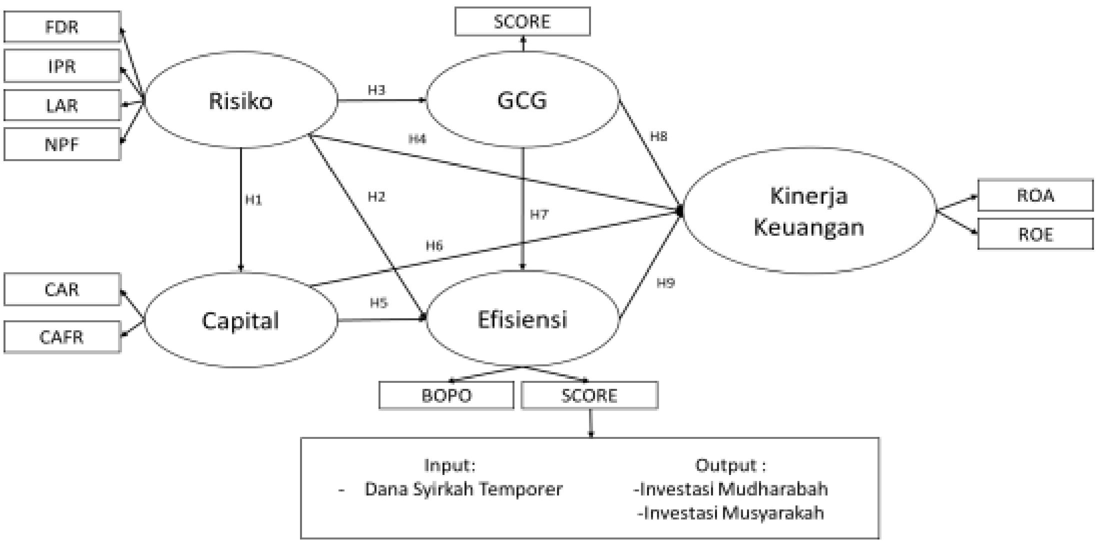

Figure 1. Conceptual Framework

III. Method

This research design was carried out quantitively. The population of the study covers fourteen syariah banks in Indonesia, and selected ten banks to represent syariah banks in Indonesia. Random sampling method was employed. These syariah banks are PT. Bank Muamalat Indonesia, PT.Bank Victoria Syariah, PT. Bank Rakyat Indonesia Syariah, PT. Bank Jabar Banten Syariah, PT. Bank BNI Syariah, PT. Bank Syariah Mandiri, PT. Bank Mega Syariah , PT. Bank Panin Syariah, PT. Bank Syariah Bukopin,PT. BCA Syariah.

The secondary data used for this study were extracted from the the annual reports of the above-listed syariah banks; the annual report covered period of 6 years, 2014 to 2019 will enable us to arrive at a rrive at a reasonable conclusion about the finance performance of Indonesian syariah banks. Furthermore, the data or information obtaind is processed using the SEM (Structural Equation Modeling) statistic method using the SmartPLS (Partial Least Square) software as a data amalysis tool.

IV. RESULT

1. Analysis Outer Model

The use of the Partial Least Square (PLS) analysis tool requires testing the validity and reliability of the contract as a test of goodness of fit on the outer model. Tests were carried out on the variables of Risk, Capital, GCG, Efficiency and Financial Performance.

Convergent Validity in PLS requires that an indicator accurately measures its construct. Testing the Convergent Validity of the outer model, by looking at the outer loading value of each indicator, is declared to be convergent valid if the loading value is > 0.5. The results of the smart PLS output for the loading factor give the results as presented in Figure 2 :

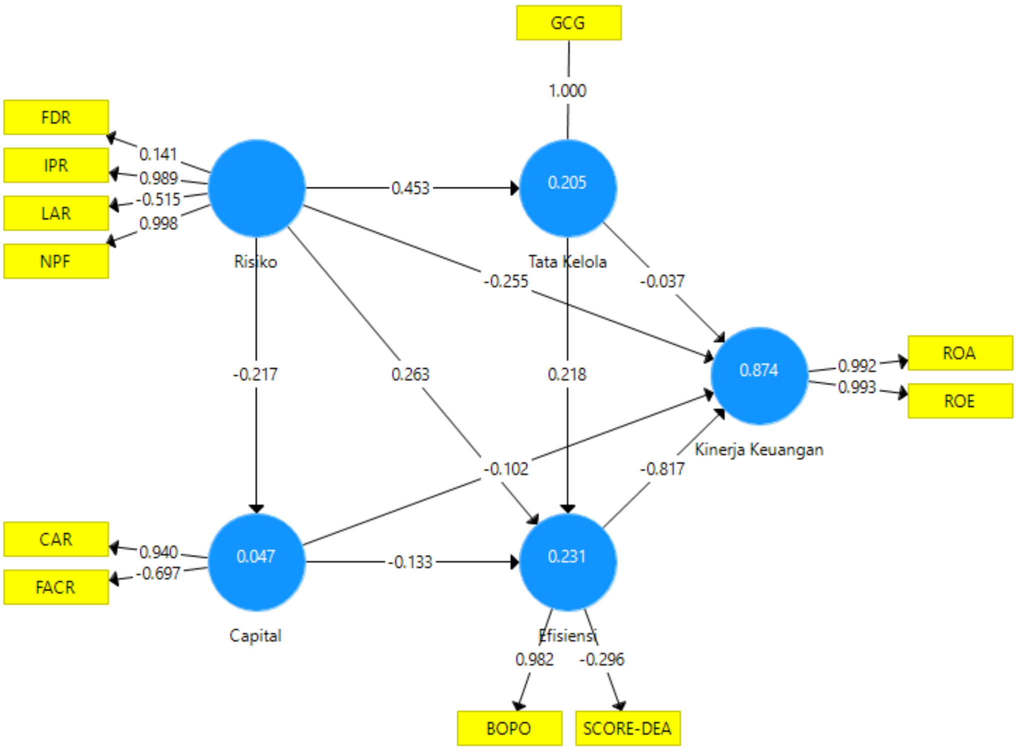

Figure 2 : Outer Model

Source: PLS data processing results

Figure 2, shows that there are four indicators that have a loading factor of less than 0.50, namely FDR, LAR which is an indicator of the risk variable, FACR which is an indicator of the Capital variable, Efficiency level (result score which is an indicator of variable i DEA) Efficiency. Four indicators that have a loading factor of <0.5 which means they do not meet the convergent requirements, so modifications are made by removing these indicators. The results of the convergent validity test after modification are presented in table 1 :

Table 1 : Final stage convergent validity test results

Variable	Indicator	Outer Loading	Explane
Risk	IPR	0,989	Valid konvergen
	NPF	0,998	Valid konvergen
Capital	CAR	0,940	Valid konvergen
GCG	GCG	1,000	Valid konvergen
Efycienci	BOPO	0.982	Valid konvergen
Performance	ROA	0,992	Valid konvergen
	ROE	0,993	Valid konvergen

Source : Result PLS

2. **Discriminant Validity**

To see discriminant validity is to look at the value of the square root average variance extracted (AVE). The recommended value is above 0.5. The AVE values obtained in this study are as presented in Table 2. Table 1 shows all the Average Variance Extracted (AVE) values above 0.5 for all variables contained in the research model. The lowest value of Average Variance Extracted (AVE) is 0.985 on the financial performance variable.

Tabel 2 : Score *Average Variance Extracted* (Ave)

Risk	0.997
Capital	1.000
GCG	1.000
Efficiency	1.000
Financial Performance	0.985

Source: PLS data processing results

3. **The Reliability Test**

The reliability test was carried out by looking at the composite reliability value of the variable. The results of composite reliability will show a satisfactory value if it is above 0.7.

Table 3 : Score *composite reliability*

Variable	*Composite reliability*	Note
Risk	0.998	Reliabel
Capital	1.000	Reliabel
GCG	1.000	Reliabel
Efficiency	1.000	Reliabel
Financial Performance	0.992	Reliabel

Source: PLS data processing results

Table 3 shows all composite reliability values above 0.7 for all variables contained in the research model. The lowest value of composite reliability is 0.992 on the financial performance variable. It can be concluded that the five variables used in this study were reliable. Based on the results of the analysis, the values of the outer loading, Average Variance Extracted (AVE) and composite reliability exceed the standards set in the model, so it can be concluded that the outer reflective model in this study has met the standard values in both validity and reliability criteri

4. **Structural Model Testing (*Inner Model*)**

Structural Model Testing (Inner Model) is carried out after the estimated model meets the criteria for the Outer model. In evaluating the structural model, measures such as R-square, Stone-Geisser Q-square test are used for predictive relevance and t-test and significance of structural path parameter coefficients.

Table 4 :Score *R-square* Model Structural

Variabel	*R-square*

Capital	0.056
GCG	0.214
Efficiency	0.210
Financial Performance	0.909

The conclusions from table 4 can be explained as follows:

a. The R-square value of the GCG variable was obtained as 0.214 or 21.4%. This shows that the GCG variable is explained by risk and capital by 21.4% and the remaining 78.6% is explained by variables other than risk and capital variables.

b. The R-square value of the efficiency variable was obtained as 0.210 or 21.0%. This shows that the efficiency variable is explained by risk and capital and GCG is 21.0% and the remaining 79.0% is explained by other variables besides risk and capital, GCG.

c. The R-square value of the financial performance variable is 0.909 or 90.9%. This shows that the financial performance variable is explained by risk and Capital, GCG, efficiency is 90.9%. and the remaining 9.1% is explained by variables other than risk, GCG capital and efficiency variables.

5. Hypothesis Testing

Table 5: Direct Effect Hypothesis Testing

Hipotesis	Variabel	*Path Coefisients*	t-statistik	*p-value*	Note
H1	Risk -> Capital	-0.118	2.591	**0.010**	Significant
H2	Risk -> Efficiency	-0.083	1.055	**0.292**	Not significant
H3	Risk -> GCG	-0.840	5.126	**0.000**	Significant
H4	Risk->Financial Performance	-0.236	1.593	**0.112**	Not significant
H5	Capital -> Efficiency	0.214	1.551	**0.121**	Not significant
H6	Capital->Financial Performance	-0.280	1.995	**0.047**	Significant
H7	GCG -> Efficiency	0.463	2.008	**0.045**	Significant
H8	GCG -> Financial Performance	0.251	0.008	**0.993**	Not significant
H9	Efficiency->Financial Performance	-0.001	5.371	**0.000**	Significant

Source: PLS data processing results

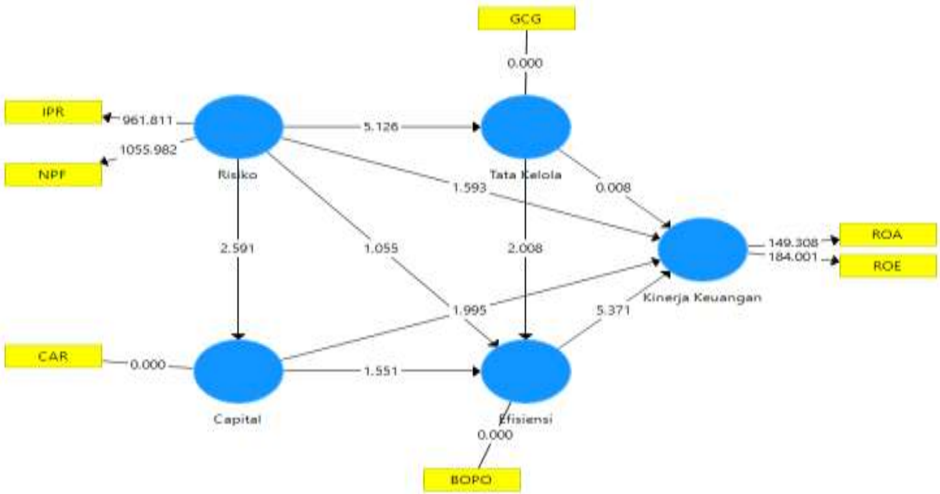

Figure 2 : Inner Model

Hypothesis testing in this study was conducted by looking at the significance of the influence between variables on the parameter coefficients and the significance value (t statistic). Hypothesis testing is carried out using the bootstrapping technique, namely recalculation of sample data at random to obtain the t statistic value on each path. The path coefficient value of the structural model is said to be significant if it produces two hypothesis tests, namely t statistic > 1.96, or p-value < 0.05. The path coefficient value of the structural model is said to be significant if it produces two hypothesis tests, namely t statistic > 1.96, or p-value < 0.05.

V. Conclusions, Implications And Recommendation

This study investigated the relevance of risk management, capital, GCG, efficiency affect to finance performance of syariah banks in Indonesia using selected banks as a representation of other syariah banks. The results of the study are that risk has a significant effect on capital in Islamic commercial banks in Indonesia; 2. Risk has no significant effect on efficiency in Islamic commercial banks in Indonesia; 3. Risk has a significant effect on GCG in Islamic commercial banks in Indonesia; 4. Risk has no significant effect on the financial performance of Islamic commercial banks in Indonesia. 5. Capital has no significant effect on the efficiency of Islamic commercial banks in Indonesia; 6. Capital has a significant effect on the financial performance of Islamic commercial banks in Indonesia; 7. GCG has a significant effect on the efficiency of Islamic commercial banks in Indonesia; 8. GCG has no significant effect on the financial performance of Islamic commercial banks in Indonesia; 9. Efficiency has a significant effect on the financial performance of Islamic commercial banks in Indonesia.

Based on the results of the analysis and testing of research conducted and discussion, suggestions that can be used as consideration for sharia banking, banking supervisors and subsequent researchers, namely:

1. For sharia banking, it is recommended to continuously improve its financial performance, namely ROA and ROE, in order to compete. In addition, to increase the amount of capital, because it has a significant effect on financial performance. It is also recommended that Islamic commercial banks implement better governance (GCG) because GCG has a significant effect on efficiency which in turn can also improve financial performance.
2. For Sharia banking supervisors, namely the Financial Services Authority (OJK), it is recommended to continue to make efficiency and capital owned by Islamic commercial banks as indicators in improving financial performance. Besides that, it is also recommended that Islamic commercial banks implement GCG because good governance affects the efficiency of Islamic commercial banks.
3. 3. For further researchers, risk indicators can be used by all indicators in risk management, especially those related and relevant to Islamic commercial banks. In addition, it is also confirmed in advance regarding the completeness of the data available at Islamic commercial banks.

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