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Bank Health, the Dividend Policy and Firm Value in Indonesia Banking Sector

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ABSTRACT: *This study aims to examine the influence of bank health towards the dividend policy and the firm value. The bank's health was reflected by the risk profile, good corporate governance, profitability and capital. The population was all banking companies listed in the Indonesia Stock Exchange, with the observation period from 2008 to 2014. The sample selected in this study was purposive sampling technique and obtained 13 sample companies. Furthermore, the data analysis and hypotheses testing applied in this study were done by a structural equation modeling approach using SmartPLS 3.0 program. The results showed that the dividend policy was affected by the risk profile and profitability of the company. However, the good corporate governance, and profitability did not affect to the dividend policy. Firm value was affected by the bank`s risk profile and profitability, compared good corporate governance and capital. Capital will affect the firm value if through dividend policy.*

KEYWORDS: *bank health, riskprofile, good corporate governance, profitability, capital, dividend policy, and firm value.*

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I. INTRODUCTION

One of the purposes of company's existence is to maximize the shareholder wealth, which can be achieved through an increase in the firm value. In the process of maximizing the value of the firm there will be conflict of interest between manager and shareholder (owner of company) called agency problem. Agency theory explains the relationship between shareholders and management described as agency relationships between principal and agency (Agency theory).The provisions on the dividends paid to shareholders require a separate policy. Increasing dividend payments indicates good prospects for the company. This will be responded by the investor to buy shares of these companies, so the company's value will increase.

Banking company is one of the companies engaged in the financial sector. Bank as an intermediary institution in the financial sector, has an important role in the economy of a country. In micro, banks function to channel funds from customers who have excess funds to business actors and individuals who need funds in order to expedite the business of the parties concerned. In macro terms, banking companies play a role as a source of financing for the development of the economy and as a means of implementing monetary policy.Askari et.al. (2012) stated that the past financial crisis has caused the increasing of asset market regulation and banking sector. The crisis happened in 2008 was the effect of banking sector condition in some countries which depleted capital quality, for that required prudence in managing the bank. The case of Century Bank is the real example known as the reference to understand and deepen the knowledge about bank health condition. In the list of stocks Indonesia Stock Exchange as of June 17, 2014 and the capitalization value indicates that of the five largest capitalization stocks, three of which were controlled by banks. Bank need to increase the ability to absorb risks caused by crisis or excessive growth in bank credit. By increasing the absorption ability of banks to risks, it is expected to create a good banking system and able to grow and compete nationally and internationally.

Regarding the bank's rating system, it can be measured based on approach to Risk-Based Bank Rating (RBBR).Bank health is a goal that all banking companies must achieve. Many previous researches include the healthy bank, dividend policy and the firm value analysis. Various results obtained may be because of the difference in research methodology and the measurement of the variables. Zameer (2013) and Eije et al. (2011) stated that risk does not significantly affect and there is no correlation to the dividend paid, while Tsuji (2012) the change of dividend policy will affect the changes of corporate risk. Bae et al. (2010), Kowalewski et al. (2007), Daradkah et al. (2013), a good corporate management is the significant determiner of dividend policy. Adediran et al. (2013), Karmau (2011), Alzomaia et al. (2013), organization dividend policy has significant positive correlation to the profitability. Afza et al. (2010), stated that between ownership structure and cash dividend is negatively correlated. Jiang et al. (2013), Fadah (2007), risk has positive effect toward firm value. Gompers et al. (2003), Kurawa et al. (2014) danObeten et al. (2014), good corporate management can create and preserve shareholder value. Albassam (2014) and Peni et al. (2011), corporate management practice does not significantly affect toward firm value. Rizqi et al. (2013), Chen et al. (2011), Charitou et al. (2010), Al Masum (2014), profitability affectsthe dividend policy.

Savitri (2012), Sujoko (2007), Jiraporn and Liu (2008), Fama and French (1998) concluded that funding decisions negatively significant affect toward the firm value. The study of the effect dividend policy toward the firm value was conducted by Chidinma et al. (2013), Yuliani et al. (2013) and Al Masum (2014).This study develops new research of healthy bank and its implication from literature study. The novelty of this model developed in this study is by the healthy bank concept which based on the indicator of Indonesian Bank and the concept of healthy bank examined by RBBR method comprehensive and integrated and it is the combination of quantitative and qualitative study in which the risk type discussed is financial risk and non-financial risk and its effect toward the dividend policy directly and indirectly. The study aims to examine the effect of healthy bank which consists of risk profile, good corporate governance, profitability and capitalization toward the dividend policy and firm value.

II. LITERATURE RIVIEW

Stakeholder Theory

Stakeholder theory is a theory focused that corporate is not just an entity operated on self-interest, but give benefit to all stakeholders (stakeholders, creditors, consumers, suppliers, government, society, analyst, and other parties). The group of stakeholder as the consideration for corporate management reveals information in the corporate report. The main benefit of stakeholder theory helps the corporate management to increase firm value as the effect of activities done and to minimize the probable disadvantage appeared by stakeholder (Ghazali and Chariri 2007).

Agency Theory

One of the relevant theories in studying the corporate governance is the agency theory. Theagency theory (Jensen and Meckling 1976) describes the relationship between the shareholders and the management of a company as the agency relation between a principal and an agent. Based on the assumption that each individual acts to maximize a self-interest, there will be difference that triggers conflict between the principal and agent. It generates the agency cost. One of the methods used to monitor the agency relationship is through the corporate governance mechanism. The perspective of the agency theory considers the corporate governance mechanism as a way to reduce the agency cost.

Tobin`s Q Theory

A corporate is valued based on the profit in the future, which reflected from relative asset risk used by corporate to generate income. James Tobin builds a theory called as Theory Q Tobin (Tobin`s q theory). The core of this theory is the monetary policy which influences economy through the effects of equity valuation.

Irrelevant Theory

Modigliani and Miller (MM) argued that value of the firm is not determined by the size of Dividend Payout Ratio, but is determined by net profit before tax (EBIT) and firm risk class. So, according to MM, dividend is irrelevant to be counted because it cannot raise the safe of shareholders.

The Bird in The Hand Theory

Gordon and Lintner (1956) stated that cost of corporate capital will rise as the effect of decreased dividend payment. Gordon and Lintner argued that investor viewed one bird in the hand is more valued than thousand birds in the air. The benefit of applying the bird in the hand theory is by giving high dividend, so the company`s stock price will get higher and will affect in firm value. The cost of company equity will rise if the dividend decreases. So, the corporate can set the high dividend payout ratio to minimize the capital cost.

Signaling Theory

In patterning signal theory, Spence (1973) utilized the labor market for signaling function model. Manager is potentially lack of information about the quality from prospective employees so that they get quality signal and decrease information asymmetry. Bhattacharya (1979) argued that if there is dividend rising, frequently followed by the stock cost rising. According to this model, only companies that perform well have ability to pay interest and dividend in long term.

MM Theory

This theory stated that capital structure does not influence the firm value. Modigliani and Miller (1961) proposed some assumptions in building his theory, such as no taxes, no broker fees, no bankruptcy fees, investor can borrow the same level as the firm, all investors have the same information with management about investment opportunity in the future, EBIT cannot be influenced by using of debt.

III. RESEARCH HYPOTESES

H1 :The risk profile has positive effect to the dividend policy
H2 : The corporate governance has positive effect to dividend policy
H3 :The profitability has positive effect to dividend policy
H4 :The capital has positive effect to dividend policy
H5 : The risk profile has positive effect to the firm value
H6 : The corporate governance has positive effect to the firm value.
H7 : The profitability has positive effect to firm value
H8 : The capital has positive effect to firm value
H9 : The dividend policy has positive effect to firm value

IV. RESEARCH METHODOLOGY

This research uses secondary data published by the companies in the annual report, financial statement, and information disclosure from the Indonesia Stock Exchange website and Bank Indonesia website. The variable is obtained from the data of the year 2008-2014. The data analysis is done by employing the Structural Equation Model (SEM) with SmartPLS 3.0. It aims to examine the relationship between variables studied and to prove the research hypotheses (Hair et al. 2009).

Population and Sample

Population is the collection of all individuals or items under consideration in a statistical study (Weiss 2012). The population of this research is 39 banking sector companies listed in the Indonesia Stock Exchange in the year period of 2008-2014. Sample is part of the population from which the information is collected (Weiss 2012). Sampling method is purposive sampling. From the whole available sample, the banking companies that have been listed in the year period of 2008-2014 are 26 companies. During the research period, there are 5 companies that listed, and 8 companies with incomplete data. Thus, the total sample is 13 companies.

Research Variables

The exogenous variable used in this research is risk **p**rofile (X_1), good corporate governance (X_2), profitability (X_3) and capital (X_4). Risk **P**rofile (RP) measured from the indicator based on the SE BI No.13/24/DPNP/2011 consist of Not Performing Loan (NPL), Derivatif toTotal Asset Ratio (DATAR), Loan to Deposit Ratio (LDR), Operational Risk (OR), Legal Risk (LR), Strategic Risk (SR), Compliance Risk (CR), and Reputation Risk (RR). The Good Corporate Governance (GCG) is measured from the indicator of practicing the corporate governance based on SE BI No. 9/12/DPNP/2007 consist of implementation of duties and responsibilities of board of commissioners (BC), implementation of duties and responsibilities of directors (DR), completeness and execution of committee duties (CD), handling of conflict of interest (CI), implementation of bank compliance function (CF), implementation of internal audit function (IA), implementation of external audit function (EA), implementation of risk management including internal control system (IC), provision of funds to related parties (RP), transparency of financial and not financial condition, GCG implementation report and internal reporting (TR), bank's strategic plan (SP). The corporate governance index is calculated by rating the number of disclosure for each indicator of the corporate governance to the expected number. Profitability (P) measured from the indicator based on the SE BI No.13/24/DPNP/2011 consist of Return on Asset (ROA), Net Interest Margin (NIM), Net Interest Income divided by the Average Total Assets (II/TA), Operating Income in addition to net interest income divided by the Average Total Assets (OI/TA), Overhead Expenses divided by the Average Total Assets (OVH/TA). Capital (C) is determined by Capital Adequacy Ratio(CAR) and Core Capital divided Risk-Weighted Assets (T1/ATMR).

The endogenous variables are the dividend policy (Y_1) and firm value (Y_2). The Dividend Policy (DP) is determined by Dividend Yield (DY) and Dividend Payout Ratio (DPR) (Niswonger 2005). The Firm Value (FV) is computed from Tobin's Q (TQ), Price to Earning Ratio (PER), and Price to Book Value (PBV) (Ehrhardtdan Brigham 2011).

V. RESEARCH AND DISCUSSION

Goodness of Fit Test

Evaluation on the Goodness of Fit for the structural model is measured by using the predictive-relevance value (*Q2*). It is calculated with the formula as follows:

$$Q2 = 1 - (1 - R1^2)(1 - R2^2)\ldots(1 - Rn^2)$$

The *R2* value for each endogenous variable is shown in Table 1.

Table 1.Results of *R*-Square

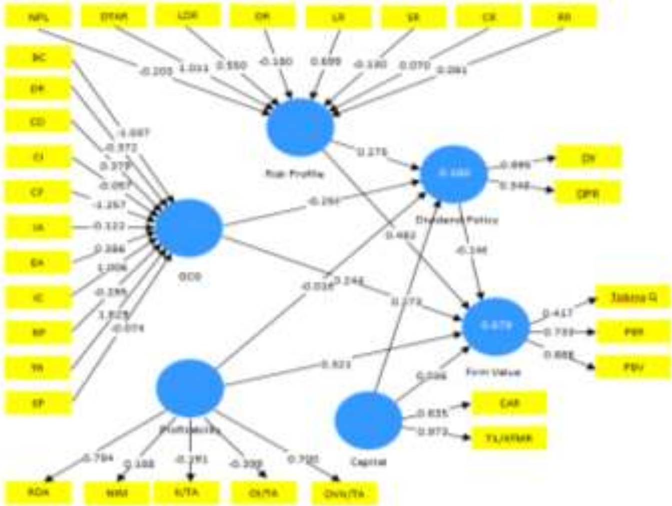
Variabel	*R Square*
Dividend Policy	0.202
Firm Value	0.695

Based on Table 1, the predictive-relevance value is 0.50412, meaning that the model is able to explain the phenomena of the dividend policy and firm value in the amount of 50.412%. The remaining 49.588% is explained by the other variables that have not been included yet into the research model and the error.

Hypothetical Testing

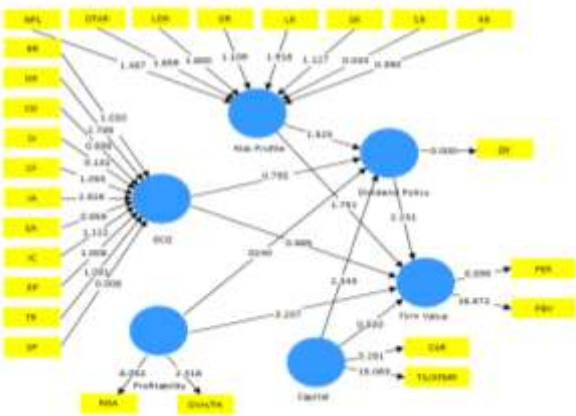
The path analysis shows the effect among the latent variables. The path analysis result is displayed in Figure 1.

Figure 1.Ouput of Algorithm in the form of Path Diagram



The hypothetical testing is done by Bootstrap resampling method, and the result is shown in Figure 2.

Figure 2.Ouput of Bootstrapping analysis in the form of Path Diagram



The result for the direct effect values can be seen in Table 2
.

Table 2. Result of The Direct Effect Values

Variable Relationship	Original Sample	P Values	Significance
RP → DP	0.314	0.064	Significant*
GCG → DP	0.311	0.213	Insignificant
P → DP	0.025	0.405	Insignificant
C → DP	0.258	0.010	Significant**
RP → FV	0.505	0.040	Significant**
GCG →FV	-0.260	0.196	Insignificant
P → FV	0.301	0.001	Significant**
C → FV	0.067	0.176	Insignificant
DP → FV	-0.187	0.013	Significant**

** signifikansi α=5%; * signifikansi α=10%

Based on path coefficient direct influence between variables in Table 2 can be explained the results of hypothesis testing as follows:

1. The result of testing of influence of risk profile to dividend policy showed path coefficient value 0,314 (positive), with value of significance (p-value) 0,064, it's mean significant at α = 10%. The coefficient positive indicates the directional relationship between risk profile and dividend policy
2. The test result of the influence of good corporate governance toward dividend policy shows the value of path coefficient of 0,311 (positive), with significance value equal to 0,213, it's mean not significant at α = 5% and α = 10%. The coefficient positive indicates the directional relationship between good corporate governance and dividend policy.
3. The result of testing of influence of profitability to dividend policy shows the value of path coefficient equal to 0,025 (positive), with p-value equal to 0,405, it's mean not significant at α = 5% and α = 10%. The coefficient positive indicates the directional relationship between profitability and dividend policy.
4. The result of capital test to dividend policy shows the value of path coefficient equal to 0,258 (positive), with significant value 0,010, it's mean significant at α = 5%. The coefficient marked positively shows the unidirectional relationship between capital and dividend policy.
5. The result of testing the influence of risk profile to company value shows the coefficient value of 0,505 (positive), with p-value equal to 0,004, it's mean significant at α = 5%. The coefficient positively shows the directional relationship between the risk profile and firm value.
6. The result of testing the influence of good corporate governance to the value of the company shows the coefficient value of the path of -0.260, with p-value of 0.196. The coefficient of negative sign shows the opposite relationship between good corporate governance to firm value and not significant at α = 5% and α = 10%.
7. Result of testing influence of profitability to company value show coefficient value of path equal to 0,301, with p-value 0,001, it's mean significant at α = 5%. The coefficient positive indicates the directional relationship between profitability and firm value.
8. The result of examination of capital effect to firm value shows the value of path coefficient equal to 0,067 (positive), with significance value equal to 0,176, meaning not significant at α = 5% and α = 10%. The coefficient marked positive indicates the unidirectional relationship between capital and firm value.
9. The result of examination of dividend policy influence to firm value shows coefficient value of path -0.187 (negative), with p-value 0.013, it's mean significant at α = 5%. The coefficient of negative sign shows the opposite relationship between dividend policy and firm value.

The indirect effect of the corporate governance to the firm value is displayed in Table 3.

Table 3.Result of Indirect Effect

Variabel Relationship	Original Sample	P Values	Significance
RP → DP →FV	-0.059	0.109	Insignificant
GCG → DP → FV	-0.058	0.202	Insignificant
P → DP → FV	-0.005	0.404	Insignificant
C → DP → FV	-0.048	0.066	Significant*

* signifikansi α=10%

Based on the results of testing the indirect effect between variables can be explained that the overall test results of indirect influence between variables have a non-significant effect for $\alpha = 5\%$, because the P Value greater than 0.05, but for $\alpha = 10\%$ capital has a negative effect significant to firm value mediated by dividend policy**.**

This research discusses the influence of bank health towards the dividend policy and the firm value. The research object is the banking sector companies listed in Indonesia Stock Exchange for the period of 2008-2014. The bank health is reflected by the risk profile, good corporate governance, profitability, and capital. The data analysis is done by employing the Structural Equation Model (SEM) with SmartPLS 3.0. The results of this study are generally as follows:

1. Risk Profile has significant influences to dividend policy. The risk profile could affect dividend paid to the shareholders. The better performance of the bank to face risk, it shows healthier the bank and finally it minimizes the risk. Management is able to manage the risks properly can be considered in General Meeting of Shareholders in determining the policies of the dividend to be distributed. The results of this study are direction with bird in the hand theory which states that investors are more willing to pay higher prices for companies paying current dividends, as current dividend payments are considered to have a lower risk of future capital gain in the future.
2. Good corporate governance has no significant effect on dividend policy. The application of banking corporate governance does not entirely follow the regulations of Indonesian Bank. Governance is considered to contribute both quantitatively and qualitatively. But this can be achieved if the implementation of good corporate governance is not just a regulatory compliance. The decision of policy whether to dividing the dividend or not in fact is determining by General Meeting of Shareholder, not based on the goodness and badness of the corporate governance. The characteristics of banking companies that implement prudential also be taken into consideration to establish the dividend policy. The results of this study support agency theory (Jensen and Meckling 1976), which states that the application of good corporate governance can help to minimize agency conflict. Good corporate governance is an instrument to overcome differences of interest (conflict of interest).
3. Profitability in banking companies has no effect on dividend policy. The condition of this anomaly in connection with during the study period global economic conditions experienced a crisis. The Bank should anticipate any possibility that may arise due to the crisis, so that although the company makes a profit but not distributed in the form of dividends to shareholders. Dividends are divided into shareholders based on the results of general meeting of shareholders, so it depends on the interest of the shareholders and not on the profitability owned by the bank. .Management is obliged to have a good financial performance, while for the determination of the dividend policy is the right of the General Meeting Shareholders. This does not support signaling theory. The net profit of the company is distributed to the shareholders in the form of dividends. Dividend distribution is one of the signals given about the condition of the company. The higher the profitability, the higher the company's cash flow, and the company can be expected to pay dividends
4. Capital positively and significantly affects dividend policy. The success of the bank lies in how banks attract public funds so as to form a strong capital and then delivered back to the community so as to form revenue for the bank. The increase in capital adequacy to cover credit risk. Increased capital firms are expected to develop the company`s operations and will ultimately increase the dividend policy. The increased capital expected to develop the company's operations and ultimately increase profits. The profit increases will have an impact on increasing the amount of dividends distributed to shareholders.
5. The risk profile positively significant affects to firm value. An increased risk of the company will affect the increased value of the company, in the short term and long term. Business banking company which is very closely with the risk should be able to channel the funds it received from the customer to manage the risk so that the risk can be impetus that banks generate higher yields. Dynamic capital market conditions prompted investors need the latest information about the company so that the company's risk significantly influences the value of the company. This support irrelevant theory by Modigliani and Miller (MM) who argue that the value of a firm is not determined by the size of the Dividend Payout Ratio, but is determined by the net profit before tax and the risk.
6. Good corporate governance does not affect the value of the company. Corporate governance both in the short term cannot affect the value of companies. In buying shares of banking companies, investors obtain information about GCG is not up to date. GCG report contained in the exchange or in the pages of companies rose after investors buy the stock, so that the information about the governance of the bank are less than helpful to investors in making investment decisions. This result not support with the signaling theory (Spence 1973). Good governance is a positive signal from the company, which can attract investors' confidence to invest, which will ultimately increase the value of the firm
7. Profitability significantly positive affects to firm value. Improved corporate profitability is followed by an increase in the value of the company. This support the signaling theory. The net profit obtained by the

company is a signal to investors indicating that the company has good prospects. Improved corporate profitability followed by an increase in the value of the company.

8. Capitalization does not affect the value of the company. The increasing of the capital is not capable of affecting the value of the company because the capital increasing is only used to cover credit risk, rather than aiming to increase its profit. On testing the indirect effect of capitalization and enterprise value which is mediated by the dividend policy a significant influence. This indicates that in buying shares of banking companies, investors do not pay attention to the capital of a bank through the company`s dividend policy. Dividend policy as a mediator between the capital and the value of the company.
9. Dividend policy negatively significant affects to the firm value. Dividend paid to shareholders, followed by an increase in the value of the company. Dividend yield is used as a banking company investor consideration in investment decisions can increase the value of companies on the stock market. Stock market prices rose as investors assume that the bank can allocate the profit generated to develop the business as additional capital to face the risks, so that the profit is not shared in the form of dividends to shareholders. The results of this study support the stakeholders theory, because it does not divide the dividend to face risks that are very closely related to the bank, so dividend policy is not only beneficial for the bank, but also for internal and external stakeholders.

This research is expected to give a contribution to stakeholders, especially businessman, issuer in banking sector, investor and candidate of investor, governance and researcher. The goodness of fit of the model in this research is 50.412% meaning that there are the other variables that have not been included yet in this study. It can be incorporated in future work.

VI. CONCLUSION

This study aims to examine the influence of bank health towards the dividend policy and the firm value. The bank’s health was reflected by the risk profile, good corporate governance, profitability and capital. Risk **P**rofile, profitability and capital measured from the indicator based on the SE BI No.13/24/DPNP/2011. The Good Corporate Governance (GCG) is measured from the indicator based on SE BI No. 9/12/DPNP/2007.
From the result of the data analysis, we can conclude as follows:

1. The risk profile influences the determination of the dividend policy and the company's value in the market, but cannot raise the risk profile of the company's value through dividend policy.
2. Implementation of good corporate company does not increase the dividend policy of banking corporate value. Banking company in Indonesia has not fully apply the principles of Good Corporate Governance (GCG) in accordance with the regulations of Indonesian Bank.
3. Profitability in banking corporate does not affect dividend policy. This anomalous condition correlates with the previous researches during 2008 – 2014, global economy condition has crisis, including banking corporate in Indonesia, so even though the company gets benefits, it is not shared in the form of dividend to the shareholders. Dividend shared to the shareholder based on general meeting of shareholders, so it depends on the interests of shareholder and not as profitability bank gained.
4. Increased capital also affects dividend policy, but the increase in capital at the banking company does not increase the value of the company. Capital will affect the capital value of the company if it is through the dividend policy. Investors buy stocks do not pay attention to the capital alone, but pay attention to capital through its dividend policy.
5. Dividend policy the feedback did raise the value of the banking company. Investors assumed that the bank can allocate the profit generated to develop the business and as additional capital to face the risks, so that the profits are not divided in the form of dividends.
6. Healthy bank little affects dividend policy because the health of the banks is not the only consideration in determining the distribution of dividends, but the health of banks affect the value of companies on the medium proportion.

This research is expected to give a contribution to stakeholders, especially businessman, issuer in banking sector, investor and candidate of investor, governance and researcher. The goodness of fit of the model in this research is 50.412% meaning that there are the other variables that have not been included yet in this study. It can be incorporated in future work.

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