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# Financial Inclusion for Economic Sustainability through the Implementation of Good Corporate Governance

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**ABSTRACT**

Good Corporate Governance is a policy that encourages the dissemination of financial products and services that are appropriate for the needs of the community. An inclusive financial policy is a deepening financial service that targets the community. Financial inclusion will encourage people to change their patterns of financial adoption and encourage economic growth. One of the indices for measuring financial inclusion is the distribution of credit funds. The aim of this study is to uncover the effect of the implementation of Good Corporate Governance toward financial inclusion for economic sustainability. This study conducted a research on some of the general banks in Indonesia. Eviews version 9.2 was employed in the panel of data analysis in this research. The samples of the data were general banks that had been registered at IDX from 2013 to 2016. The data collection was based on purposive sampling method and 108 observation data were obtained. The results of this research showed that the implementation of Good Corporate Governance bears positive effects toward the distribution of loan for consumption. In this research, the implementation of Good Corporate Governance was measured by GCG's self-assessment report.

Keywords: financial inclusion, loan for consumption, good corporate governance, economic sustainability.

## 1. INTRODUCTION

Financial inclusion is a population of a country that can effectively use banking's financial products and services. Financial inclusion is an important factor in the country's economic growth (Damodaran, 2016). Financial products and services include facilities, such as saving money in banks, borrowing money from banks, transfering money, investing and having insurance (World Bank, 2010). Financial products and services can be accessed effectively if the services provided are responsible, convenient and affordable. Accordingly, financial inclusion means sending banking services at affordable prices (Damodaran, 2016).

In their research, Ozdemir et al. (2015), found that there was a relationship between financial inclusion and financial literacy with a country's poverty level. People who possess good financial literacy will possess good decisions in using their money. A type of society that is financially well literate tends to be investment-oriented rather than consumption-oriented. One of the forms of investment is investment in education. The level of education is directly proportional to the quality of human capital. Since, the high-quality human capital is the main fuel for economic growth.

In order to support economic growth and stability, the government, through the medium of Bank Indonesia, aims to increase financial inclusion by means of inclusive financial policies. The focus of the implementation of inclusive financial policy is financial

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service deepening. The targets of inclusive financial policies are the middle and the lower classes of society with the hope of equitable access to financial banking (Bank Indonesia, 2012).

Good Corporate Governance is a process to improve a company's business and maximize shareholders' value. The banking industry business is progressing when the products can be evenly consumed by the community. The implementation of Good Corporate Governance is currently the most fundamental need in achieving the company's business targets and maintaining its existence. Moreover, competition in the banking industry and variation of products' and services' innovations bear an impact on increasingly inherent risks. However, the weaknesses of the implementation of Good Corporate Governance can lead to bankruptcy of the banking industry, especially when there is an economic turmoil (Bank Indonesia's Regulation No. 8/14/PBI/2016 on the Implementation of Good Corporate Governance for Commercial Banks).

Good Corporate Governance is one of the means to disseminate banking's products and services. Since, Good Corporate Governance is able to optimize economic results, so that it can reduce costs and have an impact on more affordable product prices (Chew and Gillan, 2005). The effectiveness of the implementation of Good Corporate Governance requires the principle of compliance in daily business activities. Consistency in implementing Good Corporate Governance must be carried out by the management, the employees, and all business people. Hence, Bank Indonesia requires banks to assess the implementation of Good Corporate Governance by using the self assessment method. (Bank Indonesia's Regulation No.13/1/PBI/ 2011 on the Commercial Bank Health Assessment).

Bank Indonesia employs three parameters in measuring the financial inclusion index. The three parameters are access, usage and quality. The "usage" parameter can be seen from the consumption of banking's products and services. There are four types of superior banking's products and services, namely depositing funds, loans, insurance and pension funds. Among the four products, loan is the main activity of the banking industry. The distribution of credit funds is a source of finance for the real sector which plays a role for economic growth (Fenstermaker and Filer, 1990).

Bank Indonesia implements an inclusive financial policy through the National Inclusion Financial Strategy (*SNKI*). The six main pillars of the National Financial Inclusion Strategy are financial education, public financial facilities, financial information mapping, supporting financial policies, supporting policies / regulations, intermediation facilities and distribution channels. Banking regulations are designed based on the suitability of banking's products with the needs of the community, however, they still pay attention to the principle of prudence. For this reason, the mechanism to distribute credit funds is made simpler with a legal basis to protect consumers (Bank Indonesia, 2012).

The financial inclusion index can be measured with the help of the "usage" parameter. The usage parameters can be measured from the number of bank's credit facilities consumed by the public. Bank Indonesia requires banks to distribute credit funds optimally from small to large loans. The large amount of credit distributed illustrates the increase in the financial inclusion index. Although credit must be channeled aggressively, the distribution must pay attention to the principle of prudence so that in the future it will not cause problems for the continuity of the banking business (Bank Indonesia's Regulation No.8/13/PBI/2006 on the Legal Lending Limit for Commercial Banks).

As described, the implementation of Good Corporate Governance or GCG, is expected to be able to support the distribution of banking's products and services to meet people's needs. Therefore, this research focuses on the effect of the implementation of Good Corporate Governance on the consumption of banking's products by the public, especially on

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the concumption of credit funds. The greater the credit funds consumed by the public shows that the bank's products are easily accessible and in accordance with the needs of the community. Thus, it can be overlooked that an increase in the financial inclusion index has an impact on economic stability.

## 2. LITERATURE REVIEW

### 2.1 Credit Loan

In their research, Chakraborty and Ray stated that banks are intermediary institutions that possess a large share in spurring the economic growth (Chakraborty and Ray, 2004). One indicator of the success of the development is economic growth, which will be directly proportional to the increase in income and increase in employment rate. Because economic growth is an absolute requirement for a successful development, the Indonesian government sets a credit growth target that must be achieved by the banks.

In accordance with Bank Indonesia’s Regulation No.8/13/PBI/2006 on the Legal Lending Limit for Commercial Banks, banks that act as drivers of economic growth must carry out their functions through the medium of real sector financing activities. Providing credit funds is an example of real sector financing. Real sector financing is performed when the banking industry operates as a provider of working capital funds, investment funds and consumption funds needed for business people in running the economy.

The distributions of credit funds by banks to debtors will be grouped by their economic sector and type of use. The distributions of credit funds based on the economic sector include the trade industries, hotel services, agriculture, mining, transportation, construction and others. While the distributions of credit funds based on the type of financing are divided based on the utilization of funds for investment, working capital and consumption.

### 2.2 Good Corporate Governance

The two main theories related to corporate governance are stewardship theory and agency theory (Wong and Bajuri, 2013). Stewardship theory is a theory that considers that the management (steward) acts to represent the company for its every interest in order to maximize the profit of stakeholders (principal). This theory assumes that basically human nature is honest, trustworthy, responsible and honorable. The company's success depends on the clarity of the vision and mission established between the management and the owner. Furthermore, stewardship theory requires the effectiveness of the company's structure as a bridge between the management's and the owner’s interests.

Corporate governance is a group of procedures implemented by directing and controlling a company with the aim of maximizing the interests of stakeholders and achieving the company’s goals (Chew and Gillan, 2005). The purpose of corporate governance is to minimize conflicts of interest that occur within the company. Broadly speaking, the objectives of GCG implementation are as follows:

1. Creating sustainability of the company
2. Maintaining company’s values and investor’s trust
3. Minimizing the agency cost and cost of capital
4. Maximizing the performance for the benefit of stakeholders
5. Protecting the company from political and legal intervention

According to the BI’s Circular Letter No.9/12/DPNP, Year 2007 on the Implementation of Good Corporate Governance for Commercial Banks, GCG was implemented based on five basic principles. First, transparency which means disclosure of relevant materials and information and openness in decision making. Second, accountability

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which means clarity of functions and implementation of accountability so that the management can run effectively. Third, accountability which means the management's compliance with applicable laws and regulations and sound banking industry principles. Fourth, independence which means professional management without the pressure and influence from other parties. Sixth, justice which means justice in fulfilling the stakeholder's rights arising from applicable legal and regulatory agreements.

According to Bank Indonesia's Regulation No.13/1/PBI/2011 on the Rating of Commercial Bank Soundness, GCG ranking is carried out through an assessment indicator in GCG using the assessment of valuations based on composite values determined by Bank Indonesia. GCG's assessment is carried out through analysis of the adequacy and effectiveness of the implementation of GCG's principles as outlined in the self-assessment work papers. The implementation of the self-assessment paperwork is carried out at a minimum in every semester, at the end of June and at the end of December.

Based on Bank Indonesia's Circular Letter No.9/12/DPNP, Year 2007 on the Implementation of Good Corporate Governance for Commercial Banks, self-assessment is based on qualitative analysis of eleven GCG's implementation evaluation factors. Furthermore, Bank Indonesia evaluates each GCG's factor using the percentage of assessment as determined by Bank Indonesia.

Each GCG's factor on the self-assessment work paper is multiplied by the assessment's percentage and summed to obtain the GCG's composite ranking classification. The GCG's composite rating consists of 5 (five) rankings, namely Ranking 1, Ranking 2, Ranking 3, Ranking 4, and Ranking 5. The smaller the ranking order of GCG's composite factors indicates the better implementation of GCG.

### 2.3 Hypothesis Development

**Financial Inclusion for Economic Substainability through the Implementation of Good Corporate Governance**

The Government of Indonesia, by means of Bank Indonesia, seeks to improve financial inclusion and financial literacy. There is a relationship between financial inclusion and financial literacy, in which people who possess good financial literacy will tend to use banking's products and services. Those banking's products and services are savings facilities, using credit funds, using interbank money transfers, having insurance and having pension funds (Bank Indonesia, 2012).

Bank Indonesia sets out a strategy to improve financial inclusion through an approach to the middle and lower classes. It is expected that all communities can obtain easy access to banking's products and services. Financial inclusion's strategical policies can be achieved by applying regulations that support and assist communities in utilizing banking's products and services. Financial inclusion means that the bank is able to provide convenience for the community in accessing banking's services and low-cost services (Damodaran, 2016).

The implementation of Good Corporate Governance is a structure implemented to achieve business growth. Its purpose is to increase shareholders' and stakeholders' value by optimizing economic results. Good GCG implementation is able to control and balance the possibility of misuse of company's resources. The impact of good corporate management causes the funds and resources borrowed by the company to be more efficient. This means that Good Corporate Governance can reduce the cost of capital so that the cost of products and services can be cheaper (Chew and Gillan, 2005).

Good Corporate Governance possesses an impact on the effectiveness of disseminating banking's products and services that are in line with the needs of the community and increases public's confidence in the banking system. The main source of

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banking income comes from the utilization of credit funds by the community. Credit funds are part of the community's financial solutions for working capital, investment and consumption needs.

Moreover, financial inclusion means banks that are able to provide financial services that are low cost and easily accessible to the public. One way to measure a country's financial inclusion index is by utilizing the “usage” parameter. The more utilization of banking’s products and services by the community, the higher the level of financial inclusion. The implementation of Good Corporate Governance causes low-cost credit facilities, consequently, the credit process is more effective and in accordance with the needs of the community. High-quality banking’s credit products are the basis for people's consideration in utilizing credit facilities from the banks.

From the aforementioned information, the hypothesis is formulated as follows:
H1: Good Corporate Governance has a positive effect toward the distribution of loan for consumption facilities.

## 3. RESEARCH METHOD

### 3.1 Population and Sample

The data used in this study was panel data. The panel data was a combination of time series data and cross section. The analysis of panel data was processed using eviews version 9.2. The data were obtained from the published reports of Bank Indonesia, Indonesian Capital Market Directory (ICMD) and the Indonesian Stock Exchange (IDX) from 2013 to 2016.

The criteria for taking the research samples were based on the following considerations: (1) banks that had been listed on the Indonesia Stock Exchange since 2013 or before 2013, (2) banks that were still operating until 2016 and (3) the complete data was available.

### 3.2 Data Types and Variables Measurements

#### 3.2.1 Independent Variable (Good Corporate Governance)

The data on good corporate governance was obtained from GCG’s implementation reports that were part of the bank's annual financial report. The method of reporting good corporate governance was self assessment. The report on the implementation of GCG published about the implementation of good corporate governance over a period of one year. The report was summarized in the GCG’s self-assessment report with GCG’s composite rating as the final result (Bank Indonesia’s Circular Letter No.15/15/DPNP dated on 29 April 2013 on the Implementation of Good Corporate Governance for Commercial Banks).

The GCG’s variable was a metric variable in the form of GCG’s score obtained from GCG’s composite rankings. The GCG’s composite rating consisted of 5 (five) rankings, namely Ranking 1, Rangking 2, Ranking 3, Ranking 4, and Ranking 5. The smaller the ranking order of GCG’s composite factors indicated the better implementation of GCG.

#### 3.2.2 Dependent Variable (Loan)

The data regarding the distribution of consumption loan facilities were obtained from notes to financial statements. The total loan distributions each year were grouped by the type of use and economic sector. The loan groups based on type of use were divided into 3 (three) credit facility choices, namely investment, working capital and consumption loan (BI’s Regulation No.8/13/PBI/2006 on the Legal Lending Limit for Commercial Banks).

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Consumer loan facilities, or often called micro credit, were given to the middle to lower class of the society. People in the middle and lower class of the community would select banks which credit processes were simple and in accordance with their needs. The variable loan measurement in this study was taken from the amount of the loan for consumption facility distributed.

### 3.2.3 Control Variable (Bank Size)

The banks' size was assessed based on the number of assets per balance sheet period in accordance to the research samples. The total assets were used as control variables because banks with large assets had more available funds to be distributed into loan facilities.

The total assets were converted in the form of natural logarithms (ln) because the independent variable other than assets was a ratio scale with a nominal number that was much smaller. Asset conversion into natural logarithms (ln) aimed to reduce deviations when the banks' size variables were regressed with other independent variables.

The measurement of the banks' size as control variables was calculated by the following formula:

$$\boxed{\text{Bank size} = \text{Ln (total asset)}}$$

### 3.3 Analysis method

The research hypothesis was tested using multiple regression analysis to measure the effect of GCG toward the distribution of loan for consumption facilities. The regression equation applied was as follows:

**Model 1:**

$$\text{Credit Loan} = \alpha + \beta 1\ \text{GCG} + \beta 3\ \text{size} + e$$

Which meant:

Credit loan: consumer's loan facilities distributed

GCG: Good Corporate Governance

Size: the size of the banks by assets

## 4. ANALYSIS AND INTERPRETATION

### 4.1 Discussions

Before the regression analysis was carried out, a sample of research panel data was tested to find out which model was the most suitable. The selection of the panel data model was carried out in two stages. First, comparing the effects of pool models with the fixed effect model. Second, comparing fixed effects models with random effects models. The panel data regression techniques were selected based on the appropriate panel data model.

After the panel data model was selected, classical assumptions were tested for panel data to determine whether the structure among individual variables (cross section) contained heterocedasticity and autocorrelation elements.

### 4.2 Hypothesis testing

**Good Corporate Governance has a positive effect toward the distribution of loan for consumption facilities.**

Model :

$\text{Loan} = \alpha + \beta 1\ \text{GCG} + \beta 3\ \text{size} + e$

The test results of the panel data model stated that the most suitable model was the fixed effect model. Furthermore, the results of the classical assumption test stated that the model

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contained heterocedasticity and autocorrelation, thus the test was carried out using a cross section weight.

**Tabel 4.1**
**Regresion of Model *Fixed Effect* Model**
***Cross-section weights* (PCSE) *standard errors & covariance* (d.f. corrected)**

Dependent Variable: LOAN?
Method: Pooled Least Squares
Sample: 2013 2016
Included observations: 4
Cross-sections included: 27
Total pool (balanced) observations: 108
Cross-section SUR (PCSE) standard errors & covariance (d.f. corrected)

| Variable | Coefficient | Std. Error | t-Statistic | Prob. |
|---|---|---|---|---|
| C | 18555490 | 3270230. | 5.674063 | 0.0000 |
| GCG? | -2186909. | 1082056. | -2.021069 | 0.0467 |
| SIZE? | 193385.5 | 84371.38 | 2.292074 | 0.0246 |

Effects Specification

Cross-section fixed (dummy variables)

| | | | |
|---|---|---|---|
| R-squared | 0.983214 | Mean dependent var | 20390178 |
| Adjusted R-squared | 0.977265 | S.D. dependent var | 31131549 |
| S.E. of regression | 4694060. | Akaike info criterion | 33.78585 |
| Sum squared resid | 1.74E+15 | Schwarz criterion | 34.50605 |
| Log likelihood | -1795.436 | Hannan-Quinn criter. | 34.07786 |
| F-statistic | 165.2639 | Durbin-Watson stat | 0.942703 |
| Prob(F-statistic) | 0.000000 | | |

Which meant:
Credit loan: consumer's loan facilities distributed
GCG: Good Corporate Governance
Size: the size of the banks by assets

The regression analysis of the panel data model showed, r-square was 0.9832 meaning that 98.32% of the use of credit loan facilities could be explained by the model. The credit loan facility was a consumption loan facility. The probability of F-statistic was significant at the 5% significance level, meaning that the regression of the independent variable on the dependent variable with the fixed model was statistically significant.

The regression results showed that GCG had a significant positive effect at the 5% significance level. Therefore, H1, GCG has a positive effect toward the distribution of loan for consumption loan, was accepted. On the other hand, the negative sign on the GCG's variable showed the opposite effect, the smaller GCG's composite factor rating indicated the better implementation of GCG.

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## 5. CONCLUSION

The results of this study indicated that GCG increased the use of credit loan facilities by the community. Loan facilities based on the type of use were divided into 3 (three) groups,

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namely investment loans, working capital loans and consumption loans. Consumer loan facilities were one type of loan facilities that was provided for lower middle class people or often called micro credit. Coresspondingly, middle and lower societies would choose banks whose credit processes were simple and in accordance to their needs (Damodaran, 2016).

The implementation of GCG was supported by 3 pillars, namely the regulators, the market participants and the business world. The government, by means of Bank Indonesia which acted as a regulator, created legislation that supported a consistent law enforcement climate. The banking industry required the business world to implement GCG a basic guideline for conducting business. In addition, the community acted as the users of banking's products and services.

GCG focused on economic efficiency which stated that the system implemented must be aimed at optimizing economic outcomes. For this reason, implementing GCG would have an impact on the costs of products and services that could be cheaper, able to control and balance the possibility of misuse of company resources (Chew and Gillan, 2005). It can be concluded that, GCG had an impact on credit loan facilities that were low cost, accessible and in accordance with community's needs.

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