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Thesis

BOARD OF COMMISSIONERS' MONITORING EFFECTIVENESS, RISK MANAGEMENT, AND SHARIA BANK PERFORMANCE IN INDONESIA

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ABSTRACT

Board of Commissioners' Monitoring Effectiveness, Risk Management, and Sharia Bank Performance in Indonesia

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This study analyzes the relationship between Board on Commissioners' monitoring effectiveness, risk management, and sharia bank performance. The samples of this research are the three general sharia banks in Indonesia. Result shows that there is insignificant relationship between the Board of Commissioners' monitoring effectiveness and sharia bank performance. Insignificant result also occurs between risk management and sharia bank performance. These insignificant results occurred due to other factors that are external to this research which brings more impact towards performance such as customer satisfaction and products and services offered by sharia banks. The reason for the insignificant results between risk management and sharia bank performance is because the rate of financing in sharia banks still remains low. Therefore risk management, represented by NPF does not significantly influence sharia bank performance. Board of Commissioners' monitoring effectiveness, based on the findings, has significant relationship towards risk management. It can be concluded that, to better implement risk management, the sharia banks should maintain their monitoring effectiveness.

Keywords: Board of Commissioners' monitoring effectiveness, risk management, performance, sharia banks.

CHAPTER 1

INTRODUCTION

1.1. Problem Background

Corporate Governance is still a famous issue to discuss since its booming in 1997. At that time, the economic situation in almost every country was poor. The preliminary developments took place in the late 1980s in the wake of corporate scandals like Polly Peck and Maxwell in the UK. A corporate governance committee, led by Sir Adrian Cadbury, came up with numerous recommendations with the publication of the Cadbury Report in 1992.

In 1995, as a response to the concerns about directors' pay and share options, the Greenbury Report suggested extensive disclosure in annual reports on remuneration and recommended the establishment of a remuneration committee comprised of non-executive directors. Again, the majority of the recommendations were endorsed by the Listing Rules. Six years later another committee published the 'Combined Code of Corporate Governance'(IIRA, 2008).

In 2001, Enron case had made people getting more aware of corporate governance matter. The fall of Enron was a direct result of failed corporate governance and consequently has led to a complete reevaluation of corporate governance practice in the United States (Munzig, 2003).

Indonesia has been successfully playing catch up in recent years on good corporate governance in terms of legislation and policies consistent with the principles and standards of internationally recognized corporate governance practices (Gingerich and Hadiputranto, 2002). It was hailed for its provisions directed towards sound corporate management and accountability when Law No.1/1995 on limited liability companies was passed after more than a decade and deliberation. The two-tier management structure of Indonesian companies was not changed. By law, the Board of Commissioners has the authority to supervise the actions and policies of the Board of Directors and to give guidance where required.

In general, the rules and principles related on Boards, is regulated in the Bank Indonesia Regulation No. 8/4/PBI/2006 for commercial banks, both sharia and conventional banks. Therefore, there is no substantial different in Boards of sharia banks and conventional banks. The different is just in article 21 on Bank Indonesia Regulation No. 8/4/PBI/2006. In the article, point (2), it is stated that the majority of Board of Directors' members shall have at least 5 years of experience in operation as an Executive Officer in a bank. On point (3), it is stated that the provision as mentioned in point (2) shall not be valid for commercial banks conducting business activities under sharia principles.

Corporate Governance is a defined set of relationships between a company's management, its Board of Directors, its shareholders and other stakeholders which provide the structure through which (i) the objectives of the company are set, and (ii) the means of attaining those objectives and monitoring performance are determined (IFSB, 2005).

CHAPTER 5

CONCLUSION

5.1. Conclusion

This research has examined the relationship between Board of Commissioners' monitoring effectiveness, risk management, and sharia bank performance of three general sharia banks operated in Indonesia, which are Bank Syariah Mandiri, Bank Muamalat Indonesia, and Bank Syariah Mega Indonesia. The research period is three years, from 2005 to 2007. These banks are chosen for their data availability and their easy to access.

Corporate governance and risk management issue in sharia banks are interesting since sharia banks are different to conventional banks. They are different in the products and service, and the most important thing is that sharia banks do not using interest rate in all of their transactions. Hopefully, this research can give contribution into literature of risk management and corporate governance of sharia banks, and give contributions in determining ways to increase performance and in making decision.

The hypothesis on the research is tested by using regression, both simple and multiple linear regressions. To do the regression, the data are processed by SPSS 14th version.

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