

CHAPTER I

INTRODUCTION

1.1 BACKGROUND OF THE STUDY

Corporate governance is defined as the structures and processes by which companies are directed and controlled. Good corporate governance helps companies operate more efficiently, improve access to capital, mitigate risk and safeguard against mismanagement. It makes companies more accountable and transparent to investors and gives them the tools to respond to stakeholder concerns. Corporate governance also contributes to development by helping facilitate new investment, access to capital, and long-term sustainability for firms, leading to economic growth and increased employment opportunities across markets. Corporate governance frameworks benefit firms through greater access to financing, lower cost of capital, better performance and more favorable treatment of all stakeholders. The sooner small businesses start adopting good practices, the more benefits they can reap. In practical terms, governance provides a key set of tools that small business can use to support their competitive survival and growth. Entrepreneurs need to start governing their companies based on a certain set of principles, trusting that specific solutions and tools will evolve with the business as it grows. For example, even simple internal controls, when properly designed, help preventing fraud and allowing for more accurate financial reporting and planning. Small business is interested in attracting investors can use better governance as a core value proposition. People perceive small businesses as lacking the ability to provide quality services and are unable to satisfy more than one critical project simultaneously due to their size and governance practices.

One critical enabling factor for small business development and enhanced business performance is corporate governance. Practicing good governance will help small business establish good business processes and prepare them for future expansion. Corporate governance determines the foundation for small business to be more accountable and transparent in their operations, thus enabling them to be more bankable and investable. Corporate governance is concerned with the decision-making processes, procedures, and attitudes that assist the company in achieving its objectives. The understanding and implementation of a good corporate governance framework presents business performance a structured path to better management practices, effective oversight and control mechanisms which lead to opportunities for growth, financing and improved performance. Corporate governance is a concept that involves practices that entail the organization of management and control of companies. It is the means by which an organization is directed and controlled. In broad terms, corporate governance refers to the processes by which organizations are directed, controlled and held accountable. Corporate governance encompasses authority, accountability, stewardship, leadership, direction and control exercised in corporations. It reflects the interaction among those persons and groups, which provide resources to the company and contribute to its performance such as shareholders and employees.

According to Mallin (2015, p.126) “the development of corporate governance will improve in institutional ownership which may lead to proper firm valuation and increasing on firm value, board decisions, and better firm performance”. Good corporate governance helps realize value and create competitive advantage. The behavior of managers show a greater performance and value of a company. Good governance refers to a combination of structures and mechanisms that align the interests of all parties involved. Good governance is

developed when structures and mechanisms are balanced, and supportive to decision-making. it seeks to ensure customer satisfaction, high employee morale and the maintenance of market which strengthens and stabilizes the company. It also provides the structure through which the company objectives are set as well as the means of attaining and monitoring the performance of those objectives. Corporate governance is used to monitor whether outcomes are in accordance with plans and to motivate the organization to be more fully informed in order to maintain or to alter organizational activity. Good corporate governance entails an efficient management of resources and provision of responsible leadership. Corporate governance controls monitor activities and then take action to accomplish organizational goals.

The governance structure of any corporate entity affects the company's ability to respond to external factors that have some bearing on its financial performance. Corporate governance is a concept, involves practices that entails the organization of management and control of companies. It reflects the interaction among those persons and groups, which provide resources to the company and contribute to its performance. The governance structure of any business entity affects the company's ability to respond to external factor. Corporate governance system helps a firm to attract investment, raise funds and strengthen the foundation for business performance. Corporate governance involves trying to establish a framework, systems and controls that encourage management to act in the best interests of the shareholders. In general, however, for business companies, corporate governance is mainly about improving business efficiency and performance.

This research is done at CV Infinity Chemical Medan. The company is engaged in distributor of chemical product. The company is established in year 2009 at Medan. The company buys the chemical

products from supplier and sells the products to customer. As distributor company, the company tries to increase the market area. The sales are done in Medan city and outside of Medan city such as Binjai, Pekan Baru and so forth. CV Infinity Chemical Medan has customers throughout Indonesia and the main business areas are paintings, coatings, adhesives, personal care, food ingredients, construction and general industrial chemicals (polyethylene, acetic acid, calcium carbonate, sodium, magnesium carbonate, trisodium and zinc sulphate) . The number of customer in year 2014-2016 can be seen as follows:

Table 1.1 The Number of Customer

Year	Amount
2014	221
2015	219
2016	197

Source : CV Infinity Chemical Medan (2018)

The company has been decreasing of business performance in year 2014-2016. It can be seen from decreasing of number of customer and sales. The company cannot make business expansion either. This problem is caused by corporate governance. The company doesn't change in corporate governance structures that are expected to bring out positive result on business performance. Owners that are more familiar with the company's activities cannot control the business activities. The owner doesn't have motivation to control the employee that cannot work optimally in achieving the company's goal. The company doesn't have clear reporting lines and clarity about how decisions are made and how risks are controlled, and about other matters that need to be brought to the owner's attention for review or approval. The company doesn't promote understanding of roles and responsibilities and limits of authority and set the balance the owner wants to see between acceptable risk and reward. The employee doesn't get good reward based on the performance. Any incentives for employee need to be given based on performance. The company

doesn't support a clear communication between the owner with employee. Appropriate internal controls aren't established related to key risks. Owners need to have good control of company's activities and decision making which includes the provision of high quality information on business performance and risk management.

Based on description above, the writer wants to conduct the research with title **“The Impact of Corporate Governance on Small Business Performance at CV Infinity Chemical Medan”**.

1.2 PROBLEM LIMITATION

Due to limitation in time and ability, the writer determines problem limitation on corporate governance as independent variable (X) and business performance as dependent variable (Y). The research is done on CV Infinity Chemical Medan at Jln. Taruma No. 23 Medan. Indicators of corporate governance are clear strategy, effective risk management, discipline, fairness, transparency, social responsibility and self evaluation. (Dzama, 2015, p.369). Indicators of business performance are time, quality, productivity, flexibility and environmental. (Amaboldi, et.al., 2015, p.51)

1.3 PROBLEM FORMULATION

Based on the background study above, the writer can take problem formulation as follows : Does the corporate governance have impact to business performance at CV Infinity Chemical Medan?

1.4 OBJECTIVE OF THE RESEARCH

The purposes in doing this research are to know whether there is the impact of corporate governance to business performance at CV Infinity Chemical Medan.

1.5 BENEFIT OF THE RESEARCH

The benefits from conducting this research are as follows:

1.5.1 THEORETICAL BENEFIT

1. For writer, this research can provide an additional knowledge and experience for writer in entrepreneurship especially corporate governance and business performance.
2. For other researcher, this research can be used as reference to next research that is related with this research topic.
3. This research will give a contribution in developing entrepreneurship theory.

1.5.2 PRACTICAL BENEFIT

1. For the company, this research can provide suggestion to company in improving business performance with corporate governance.
2. For the other entrepreneur, this research can give the input in implementing the corporate governance for the increasing the business performance.

1.6 SYSTEMS OF WRITING

The systems of writing in this *skripsi* will be as follows :

Chapter I : Introduction

In this chapter, the writer describes about the background of the study, problem limitation, problem formulation, objective of the research, benefit of research and systems of writing.

Chapter II : Literative Review and Hypothesis Development

In this chapter, the writer describes some theories that are related to the topic of the study, such as definition of corporate governance, element of corporate governance, importance of corporate governance, benefit of corporate governance, implementation of corporate governance, indicator of corporate

governance, definition of business performance, the way in improving business performance and indicator of business performance. The writer presents previous research, develops hypothesis, makes research model and framework of thinking.

Chapter III :Research Methodology

In this chapter, the writer explains the research design, population and sample, data collection method, operational variable definition and variable measurement and data analysis method.

Chapter IV :Data Analysis and Discussion

This chapter consists of general view of research object, data analysis and discussion.

Chapter V :Conclusion

This chapter contains the conclusion, the implication and recommendation of this research.

