CHAPTER I
INTRODUCTION

1.1 Background of Study

The performance of a company can be deliberated in several ways by implementing different methods. However, one of the most commonly methods used refers to financial analyses that target the profitability in determining the overall performance and efficiency. Profitability and financial performance could be used to clarify the company's polices and operations in monetary term. Under the Generally Accepted Accounting Principle (GAAP), financial statement can be categories into Income Statement, Balance Sheet and the Cash Flow Statement. The Income Statement contains information about the revenue and expense of the company. Moreover, the total assets that equals to the total liabilities and shareholder's equity can be seen from the Balance Sheet. The Cash Flow Statement also reveal how company record their cash flow activities within a certain period of time.In evaluating the overall financial condition, the income statement and balance sheet in the financial statements play a significant roles, as it capture the overview the company's operating performance.

Financial statements are a form of accountability from the management to the shareholders. These financial statements provide information needed by shareholders and prospective investors to make decisions in investing their funds. The financial statements can be record and prepare by using two accounting methods such as Cash basis and Accrual basis method. The cash basis method are prepared by recognizing every income and expenses according to the real-time cash flow. On the contrary, the accrual basis method record the revenue and expenses when they are incurred. Although the cash basis method present the simple ways on analyzing the cash flow, there are limited user toward the method such as the small nonmanufacturing business and the business that do not make many financial disclosure to the IRS. As the business grows, it is recommended for business to shift into the accrual basis method as it capture more precise measure of the companys productivity.

The income statement in financial statements are the main information that help to determine the investors decision. The management is the most responsible party and concerned in the company's performance, the management will definitely try to decrease any fluctuations in order to maintain the company profits. The managers along with the accountant will go thru the financial statement and relegate any costs that could contribute into decreasing profit. Earnings information as part of financial statements, is often the target of engineering through management's opportunistic actions with the purpose of maximizing satisfaction, but this action can harm shareholders or investors because the profit information presented can lead to wrong investment decisions.

Opportunist action is an action done by choosing certain accounting policies, so that the company's profits can be accustomed, increased or lowered according to the management wishes. Likewise, the management can also regulate profits according to their wishes in terms of earnings management. If in a condition where management does not succeed in achieving the predetermined profit target, the management will utilize the flexibility allowed by accounting standards in preparing financial statements to modify reported earnings management, in order to show good performance in generating value or maximize profit for the company. Therefore, the management tends to choose and apply the accounting method that can provide a better profit information.

Earnings management appears as the impact of agency problems that happen because of inconsistencies interests between shareholders(principal) and company management(agent). The shareholder(principal) is motivated to prosper himself with the increasing profit while agents are provoked to maximize the fulfillment of needs of economic and psychological, among others in terms of obtaining investment, loans, as well as compensation contracts. In such conditions, a control mechanism is needed so that can help to align differences in interests between the both parties.

According to agency theory, to overcome the problem of inconsistency of interests between the principal and the agent can be done through good corporate management. Good corporate management can be define as ways on improving a mutual support and efficieny between the company and the employees in order to achieve their goals. Good corporate governance has the purpose to protect the company's managers always take appropriate actions and selfless, along with the company's stakeholder.

Managerial share ownership is ownership of shares owned by executives and directors. The ownership is determined by the percentage of the number of shares over the entire shares of the company. Someone who owns shares of a company can be alleged to be the owner of the company even though the number of shares own is only a few sheets. Managerial ownership can be measured by the amount of share ownership by the management of the company to the total number of shares outstanding.

Board composition refers to the number and type of commissioners in a company which is usually referred as insideoutside commissioners. Insider or insiders are permanent members of the top management team and are also employees of the company concerned. While outsider or outsiders are independent members who have no such relationship. Outsiders are usually called independent commissioners. The composition of the board is only focused on the board of commissioners represented by commissioners as parties that have connections with the majority shareholders and independent commissioners as parties that do not have a connection with either the majority shareholders or with company management.

Company size is a determination of the size of the company. The higher total assets of a company shows the greater amount of assets owned by the company and that indicate that the company is categorize as a large company. And conversely, the lower total assets indicate that the company categorizeinto a small company. Along with the greater total assets indicate that the greater the assets owned by the company, it will also attract the investors to invest and be more secure to invest into the company. Company size is measured using Ln total assets and the size of the company is proxied by the total assets of the company every year. Companies with large assets will use the available resources as much as possible to generate maximum business profits and on the other sides, companies with small assets will also generate profits in accordance with their relatively small assets.

Profitability is the company's ability to generate a profit. The greater the level profitability of a company shows that the company is able to survive in the market, hence the company is able to improve the managerial ownership structure and composition of the board in a broader annual report.

The company used as the object of this research is the food and beverage companies registered in Indonesia Stock Exchange. Food and beverage companies can be define as companies that involved into processing raw materials, packing and distributing the final products. The final products produced are meant for the human consumption can be categorize as the food and beverage industries.Currently, the food and beverage industries had become the most promising industries as the increasing in health conscious and the growth of urbanization lifestyle.

To sum up, managerial ownership and board composition as part of good corporate governance along with the firm size take part in determining the influence toward firm's profitability.

Besides of the influence of Managerial Ownership, Board Composition and Firm Size towards the Profitability, according to Kasmir (2012: 89), there are severeal factors that influence profitability that include as Net profit margin, Total asset turnover, Net profit, Sales, Total Assets, Fixed Assets, Current assets and Total Cost.

Based on the explanation above, researchers present phenomena data about the sales growth, working capital, receivable turnover and liquidity in the some pharmaceutical companies in year 2013-2017that can be seen as follows:

Table 1.1 Managerial Ownership, Board Composition, Firm Size and Company's Profitability in Year 2013-2017

Company	Year	Managerial Ownership	Board Composition	Firm Size	Company's profitability
PT. Tunas Baru Lampung Tbk	2013	0,1 %	9	15,64	1,36
	2014	0,08 %	9	15,81	5,91
	2015	0,08 %	9	16,04	2,12
	2016	0,08 %	9	16,35	4,89
	2017	0,08 %	9	16,46	6,77
PT Kino Indonesia Tbk	2013	10,5%	8	14,10	14,76
	2014	10,5%	8	14,44	10,98
	2015	10,5%	8	14,98	8,19
	2016	10,58%	9	15	5,50
	2017	10,6%	9	14,99	3,41

Source : Indonesia Stock Exchange (2019)

From table above, the financial statements in PT Tunas Baru Lampung Tbk and PT Kino Indonesia Tbk shows that inconsistent change of profitability in year 2013-2017. It can be seen that in year 2014-2015 there was an increase in the size of the both company, however the managerial ownership and the size of the board remain unchanged but at the same time the net profit actually declined.

Based on the background study above, the researcher is interested in choosing the title of**"The Influence of Managerial Ownership, Board Composition and Firm Size Towards Profitability in Foods and Beverages Companies Listed in Indonesia Stock Exchange"**

1.2 Problem Limitation

In this study, it emphasized on independent variable such as Managerial Ownership, Board Composition and Firm Size and the dependent variable is Profitability. This study is conducted to examine the effect of Managerial Ownership, Board Composition and Firm Size on Profitability.The research focuses on the financial statements each of the company. In all 6 companiesfoods and beverages were used for the research in 5 periods for 2013-2017.

1.3 Problem Formulation

Problem formulation in this research are as follows:

1. Does managerial ownership partially influence profitability on Foods and Beverages Companies 2013-2017?
2. Does board composition partially influence profitability on Foods and Beverages Companies 2013-2017?

3. Does firm size partially influence profitability on Foods and Beverages Companies 2013-2017?
4. Do managerial ownership, board composition and firm size simultaneously influence profitability on Foods and Beverages Companies 2013-2017?

1.4 Research Objective

The objective of doing this research are as follows:

1. To analyze the influence of managerial ownership toward profitability in food and beverage companies on the Stock Exchange partially for the 2013-2017 period
2. To analyze the influence of board composition toward profitability in food and beverage companies on the Stock Exchange partially for the 2013-2017 period
3. To analyze the influence of firm size toward profitability in food and beverage companies on the Stock Exchange partially for the 2013-2017 period
4. To analyze the influence of managerial ownership, board composition and firm size toward profitability in food and beverage companies on the Stock Exchange simultaneously for the 2013-2017 period.

1.5 Benefit of the Research

The benefits from conducting this research are as follows:

1.5.1 Theoretical Benefit

a. For writer

The research is used to enhance the knowledge of how significant the influence of Managerial Ownership, Board Composition and Firm Size toward Profitability in Food and Beverages Industries.

b. For the company

The result of the research hopefully can be useful as reference and insight about the importance of the influence of Managerial Ownership, Board Composition and Firm Size in Food and Beverages Industries.

1.5.2 Practical Benefit

a. For future research

The research could be the additional guideline or referenes for future researcher who are interested on conducting the same theory.

b. For the company

The research will give knowledge about the influence of Managerial Ownership, Board Composition and Firm Size toward Profitability in Food and Beverages Industries.

1.6 Systems of Writing

In the systematics of writing. the author will briefly describe the chapter by chapter in sequence. The order of writing the chapter to be presented is as follows:

Chapter I : Introduction

This chapter consist of thebackground of the study, problem limitation, problem formulation, objective of the research, benefit of the research (Theoretical and Practical benefit) and systems of writing

Chapter II: Literature Review and Hypothesis Development

This chapter explaining further about the theory that covers about theoritical background used in this research is agency theory along with explaination about Managerial Ownership, Board Composition, Firm size and Profitability. Some summary of the selected previous research will be mentioned in this chapter, hypothesis for this research is also briefly explained through the figure of research model.

Chapter III : **Research Methodology**

This chapter describe about the research design, population and sample, data collection method, operational variable definition and variable measurement, as well as data analysis method. The data analysis used for this research descriptive statistic, classical assumption test, multiple regression analysis and hypothesis through t test and F test.

Chapter IV : **Data Analysis and Discussion**

This chapter consist of the general view of the research object, Data analysis (Descriptive statistic, Result of data quality testing and Result of the hypothesis testing) and Discussion. All the collected data will be testified through the data analysis method mentioned in Chapter III and the conclusion will be made based on the criteria set for each certain test.

Chapter V : **Conclusion**

The last chapter comprises the conclusion made from whole research test, beside the conclusions, the writer also make some implication and recommendation which can be useful for the future research to conduct the same are of study.