

# CHAPTER I

## INTRODUCTION

### 1.1 Background of the Study

Firm value is the view of investors on the company, and this is often associated with stock prices as well as a company's financial growth. Stock price is meant by the price that occurs when shares are traded on the stock market. If the stock price is high, the firm value will also be followed by high figures. On the other hand, firm value is the result of management from various sectors, including capital structure, financial performance, and credit quality. As stock price is one of the indicators towards firm value, this applies to companies especially banking companies that are already listed on the stock exchange where the amount of stock prices will affect the company. This is an indicator of firm value and potential investors before deciding to become an investor in a company.

As a finance company, banks must pay attention to careful planning in making funding decisions. The bank's capital structure is how the bank finances its business and operations. The bank's capital structure is characterized by a much higher level of debt (Irdavani, 2015). This is reflected in the international regulation in the banking sector, namely Basel III. The regulation states that banks must maintain a capital adequacy ratio of no less than 8%. The capital structure of a bank includes high

leverage, so there is a risk if the bank goes bankrupt for some reason. One of the risks of bank failure is the high number of bad loans. Non-Performing Loans (NPL) are loans that are past due for 90 days or more and include bad loans, substandard loans and doubtful loans. Non-Performing Loan is one of the indicators for assessing the performance of banking functions. With good credit management and the use of prudential principles, the bank can increase the value of the company and generate a better profit value for the company. Return of profit based on Assets as well as beneficial compared to other indicators. The more return a company gain would also sending a signal to potential investors to invest in the company.

Banks are financial institutions that focus on saving deposits on demand, reserves and time deposits. Moreover, the bank is also regarded as a spot where people can buy money, sell money, transfer money, or collect payments of all sorts. Banking as a financial institution has an important role in the life of a country, especially in a developing country like Indonesia. The strategic role of the bank is mainly due to the main function of the bank as an institution that can raise funds and channel public funds effectively and efficiently.

Banks are the most important financial institutions in a country that affect the economy both at macro and micro levels. In Indonesia, banking, both consumption and investment, has a market share of 80% of the total financial system currently available (Winarto, 2020). Banks in running their business collect funds from the public and channel them back into various investment alternatives. In connection with this

function of collecting funds, banks are often called trust institutions. In line with these business characteristics, the bank is a business segment whose activities are largely regulated by the government. There are two types of banks in Indonesia, including conventional banks and shari'ah banks. Shari'ah banks are banks whose activities leave us with a problem of usury (*riba*).

The Banking Industry in Indonesia is supervised by an agency called the Financial Services Authority (OJK). OJK has the function of administering an integrated regulatory and supervisory system in the financial services sector, which is divided into the banking sector, capital market and non-bank financial industry. Banks carry out their functions based on the principle of prudence. The main function of banking is to collect and channel public funds with the aim of supporting the implementation of national development in the context of increasing equitable distribution of development and its results. Banking is also one of the pillars of economic growth and national stability to improve people's lives in terms of the financial sector.

According to OJK data as of March 2020 the number of banks was 96 banks which were divided into 4 categories from Commercial Banks based on Business Activities (BUKU). The distribution includes 12 banks of BUKU I, which is a bank with core capital of 100 billion rupiahs to 1 trillion rupiahs, 52 BUKU II bank which has a core capital of 1 trillion rupiahs to 5 trillion rupiahs, 26 BUKU III bank which

has a core capital above 5 trillion rupiahs to 30 trillion rupiahs, and 6 BUKU IV banks with core capital above 30 trillion rupiahs.

There are several measurements used to measure the firm value of the company, some of which are used are divided into: Capital Adequacy Ratio is a ratio that serves to accommodate the risk of loss that may be faced by the bank. Capital structure is a balance or comparison between capitals that is sourced by our own capital and foreign source of capital. Non-Performing Loan (NPL) is a ratio used to measure a bank's ability to cover the risk of credit failure by debtors. Return on Assets (ROA) is a ratio used to measure the ability of bank management to obtain profits or overall profits.

**Table 1. 1**  
**Comparison Table of Top Four Best Performing Banking Company in Indonesia**

No.	Year	Stock Code	CAR	DER	NPL	ROA	PBV
1.	2017	BBRI	21.95%	5.71	0.88%	2.57%	2.66x
	2018		20.15%	6.00	0.92%	2.49%	2.44x
	2019		21.52%	5.79	1.04%	2.43%	2.60x
	2020		19.59%	6.56	0.80%	1.23%	2.57x
2.	2017	BMRI	21.64%	5.62	1.06%	1.91%	1.10x
	2018		20.96%	5.50	0.67%	2.15%	1.86x
	2019		21.39%	5.31	0.84%	2.16%	1.73x
	2020		19.90%	6.38	0.43%	1.23%	1.52x
3.	2017	BBCA	23.1%	4.71	0.4%	3.11%	4.07x
	2018		23.4%	4.44	0.4%	3.13%	4.18x
	2019		23.8%	4,28	0.5%	3.11%	4.68x
	2020		25.8%	4.82	0.7%	2.52%	4.52x
4.	2017	BBNI	18.5%	6.03	0.7%	1.92%	1.81x
	2018		18.5%	6.33	0.8%	1.86%	1.47x
	2019		19.7%	5.76	1.2%	1.82%	1.16x
	2020		16.8%	6.90	0.9%	0.37%	1.02x

Source: Prepared by Writer (2021)

Table 1.1 above contains information related to the Capital Adequacy Ratio, Debt-Equity Ratio, Non-Performing Loan, Return on Assets, and Price to Book Value

of 4 companies that have the best banking performances in Indonesia. These 4 companies are consisted of Bank Rakyat Indonesia (Persero) Tbk, Bank Mandiri (Persero) Tbk, Bank Central Asia Tbk, and Bank Negara Indonesia (Persero) Tbk.

In the last few years, the banking performance in Indonesia tends to be far from the expectations of the stakeholders. To meet the expectations of the stakeholders, government is carrying out banking recovery and restructuring in order to improve banking performance in Indonesia so that it is of good quality. The performance of this bank has various problems due to intense competition. Financial performance in particular that really needs to be improved in order to improving the firm value of a banking company. Assessment of banking financial performance can be identified in various ways, one of which is using the banking-related Financial Ratio.

Using financial indicators such as Capital Adequacy Ratio, Capital Structure, Non-Performing Loan, and Return on Assets, this research is expected to increase knowledge and be able to find out how these variables affect the firm value towards the banking industry in Indonesia. Seeing the importance of discussing and analyzing these variable to determine the firm value of bank that established and listed in Indonesia, the writer took the title **“The Impact of Capital Adequacy Ratio, Capital Structure, Non-Performing Loan, and Return on Assets Towards Firm Value of Banking Companies Listed in Indonesia Stock Exchange”**.

## 1.2 Problem Limitation

The writer has set a few problems in order to prevent differences from the subject.

This include:

1. The Research will use Capital Adequacy Ratio to measure financial performance
2. The Research will use Capital Structure to measure financing, composition, and leverage
3. The Research will use Non-Performing Loan to measure loan or credit
4. The Research will use Return on Assets to measure profitability
5. The Research is using banking companies listed in IDX from year 2017 to 2020 as the object

## 1.3 Problem Formulation

Based on the background and determination of problems above, the formulation problems are written as follows:

1. Does Capital Adequacy Ratio have an influence towards the firm value of a banking company listed in Indonesian Stock Exchange?
2. Does Capital Structure have an influence towards the firm value of a banking company listed in Indonesian Stock Exchange?

3. Does Non-Performing Loan have an influence towards the firm value of a banking company listed in Indonesian Stock Exchange?
4. Does Return on Assets have an influence towards the firm value of a banking company listed in Indonesian Stock Exchange?
5. Does Capital Adequacy Ratio, Capital Structure, Non-Performing Loan, and Return on Assets have an influence towards the firm value of a banking company listed in Indonesian Stock Exchange simultaneously?

#### **1.4 Objectives of the Research**

The research objectives are determined as follows:

1. To determine whether Capital Adequacy Ratio affects changes in the firm value of a banking company listed in Indonesian Stock Exchange.
2. To determine whether Capital Structure affects changes in the firm value of a banking company listed in Indonesian Stock Exchange.
3. To determine whether Non-Performing Loan affects changes in the firm value of a banking company listed in Indonesian Stock Exchange.
4. To determine whether Return on Assets affects changes in the firm value of a banking company listed in Indonesian Stock Exchange.
5. To determine whether Capital Adequacy Ratio, Capital Structure, Non-Performing Loan, and Return on Assets simultaneously affects changes in the firm value of a banking company listed in Indonesian Stock Exchange.



## **1.5 Benefits of the Research**

Based on the research objectives to be achieved, this research is expected to have benefits in multiple fields, either directly or indirectly. The benefits of this research are as follows:

### **1.5.1 Theoretical Benefits**

Theoretically, the results of this study are expected to be useful for:

- a. Literature material for theoretical studies and references for other students or academics that are interested to conduct a further research related to firm value of a banking company.
- b. Increase knowledge and insight on the details of the effects or influence of capital adequacy ratio, capital structure, return on assets, non-performing loan, and return on assets toward firm value of a banking company.

### **1.5.2 Practical Benefits**

Practically, this research can be useful as follows:

- a. For Educators and Prospective Educators

It is expected that the research is able to provide additional materials for the educators in order to increase the knowledge or conducting their research on the related field of study.

- b. For Companies



The result of this research is expected to provide and supply an essential information for the company regarding the factors affecting their financial performance, mainly on capital adequacy ratio, return on assets, and capital structure.

c. For Investors and Prospective Investors

The research is expected to provide and supply information regarding the financial condition and financial performance of the companies, mainly the related study conducted in this research. In addition, the results of this research can also use as a material for consideration in an investment-related decision making to a company.

