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THE IMPACT OF FOREIGN SHAREHOLDINGS, FOREIGN COUNTRY ADVANCEMENT, AND CORPORATE GOVERNANCE MODERATING ROLE ON BANK EFFICIENCY

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Research Highlights

This research is intended to open a new perspective on how foreign shareholdings in Indonesia's banking industry affect the efficiency of its acquired local banks by analyzing the foreign shareholdings percentage/portion and also analyzing its country of origin that till date is still scant. The results of the studies show that percentage of foreign shareholdings positively affecting efficiency of acquired local banks only if the foreign shareholders is majority shareholders and originating from developed countries. The increase in the size of the Board of Directors tends to decrease the efficiency of the acquired local banks and lastly, the presence of Foreign Director has a positive moderating effect on strengthening the effect of percentage of foreign shareholdings on the efficiency of the acquired local banks. The original contribution of this studies is that the percentage of foreign shareholdings and its country of origin are two factors that cannot be separated in affecting the level of efficiency of its acquired local bank.

Graphical Abstract

Estimation Results using EGLS

	Efficiency	t-statistic	Probability
C	0.506742**	2.044	0.0418
AsiaD	0.100263***	3.279	0.0012
Asia	-0.028224	-0.749	0.4547
China	-0.733912**	-2.030	0.0432
CGD	-0.010969**	-2.037	0.0425
CGF	-0.018406	-1.565	0.1184
CGDAsiaD	-0.010868***	-3.221	0.0014
CGDAsia	-0.014144***	-2.740	0.0065
CGDChina	0.072183	1.247	0.2134
CGFAsiaD	0.025352***	3.221	0.0014
CGFAsia	0.051853***	2.740	0.0065
CGFChina	0.041118	0.395	0.6935
ROA_{t-1}	0.030183***	6.489	0.0001
LNASSET	0.045563***	2.777	0.0058
CAR(%)	0.000714	1.488	0.1379
INFL(%)	-0.00236	-0.632	0.5278
GDP(%)	-0.050278***	-3.385	0.0008
D1	0.004063	0.138	0.8901
R square	0.366023		
Adjusted RSq.	0.330217		
F statistic	10.2224		
Prob.(Fstat.)	0.00000		
DurbinWStat.	1.4074		

***significant at α < or = 1%, ** significant at α >1% or < 5%, and * significant at α >5% or <10%

Source: Calculated by using E *Views* 10

Whereas:

Asia D is percentage ratio of foreign shareholding of developed countries in bank i at year t.

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Asia is percentage ratio of foreign shareholding of developing countries at bank i at year t.
China is percentage/proportion ratio foreign shareholding of China in bank i at year t.
ROAt-1 is the profitability of previous one year of bank i at year t as time lag of approximately 1 year is required by bank to allocate its resources efficiently to obtain higher profit.
CAR is the ratio of the capital on risk-weighted asset of bank i at year t.
CGD is numbers of the member of Board of Directors (BOD).
CGF is numbers of foreign Director/Commissioner.
CGDASIA is moderating variable of numbers of BOD.
CGFASIA is moderating variable of Foreign Director.
D is the Dummy variable to see the efficiencies of the acquired local bank after global crisis. D = 0 (2007-2008) dan D =1 (2009-2017).

Research Objectives

The aim of the study is to investigate the impact of foreign shareholding originated from developed and developing countries on the efficiency of acquired local banks in Indonesia during 2007-2017 by including Corporate Governance as moderating variable. In this paper, we will develop a formal model to analyze the impacts of foreign shareholdings concentrations on bank efficiency based on the country of origin of the investing banks by including Corporate Governance as a moderating factor. The model is tested using recently available data from the Indonesian Banking Directory. As most of the growth of acquisition of local banks by foreign investors has occurred in the recent years during the past decade after the issuance of the government regulation permitting of 99% foreign shareholdings, therefore, explaining the facts during the decade will explain much of the total phenomena. The research questions to be addressed in this study is first, whether the percentage or portion of foreign shareholdings affects the bank efficiency. Second, whether the country economic development of the foreign shareholders affects the efficiency of the acquired local banks and the third, whether Corporate Governance represents as moderating factor by strengthening or weakening the relationship between foreign shareholdings and bank efficiency.

Methodology

Using the secondary aggregate data of 29 commercial banks acquired by foreign shareholders in 2007-2017 obtained from central bank of Indonesia and World Bank/IMF databases, a panel regression model using Generalized Least Square (GLS) and DEA was applied to examine the effects of percentage of foreign shareholdings from developed countries, developing countries and China on efficiency of the acquired local banks. GLS is a least square techniques designed to overcome heteroscedasticity which is able to preserve the efficiency of the estimator without losing its unbiased and consistency characteristics. GLS is able to minimize residual square which has been weighted (weighted least square) so it can fulfill the standard assumptions of the least square (OLS) resulting in the BLUE results estimations (Gujarati dan Porter, 2012). We adopt the profitability approach to determine the input and output vectors for estimating efficiency instead of intermediation or production approach due to the; First, Drake et al, 2009 conclude that profitability approach will give more comprehensive analysis because different interest rate factor and risk transfer factor has been included in the analysis. Whereas other

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approach does not incorporate the different interest rate factor completely and lack of including the risk transfer.

Results

The average percentage of foreign shareholdings of developed countries of 62.8% (calculated separately) which is relatively high is significantly increasing efficiency. This result is supported by a study by Ozili and Uadiale, 2017 conclude that the high percentage of shareholding in the bank will increase its net interest margin or efficiency. Whereas the low average percentage/portion of foreign shareholdings from developing countries of 23.4% (calculated separately) has no impact on efficiency. Therefore it is concluded from this study that the percentage of foreign shareholding will affect the efficiency of its local acquired bank only if the foreign shareholdings is majority shareholders and is originated from developed countries. The same results made by Phung and Lee 2013; Whitley and Kristense 1996; Gedajlovic, Yoshikawa and Hashimoto 2004. This is due to the better managerial skills, expertise, technology, and performance of the developed countries as opposed to developing countries (Yong and Chan, 2016). The increase in the size of the Board of Directors will significantly decrease efficiencies of the acquired local banks. These findings is consistent with study made by Lipton and Lorsch, 1992 which suggests that smaller board size is beneficial for driving organizational outcomes . The increase of number of Foreign Director in the acquired local bank by foreign shareholders will have positive impacts and significant in increasing efficiency of the acquired banks. These results show that Foreign Director is a significant moderating variable in strengthening the effect of foreign shareholdings on efficiencies of the acquired local banks.

Findings

The main findings of the studies is that percentage of foreign shareholdings positively affecting efficiency of acquired local banks only if the foreign shareholders own majority shareholdings and originating from developed countries. Increasing size of the Board of Directors tends to decrease the efficiency of the acquired local banks and lastly, the presence of Foreign Director has a positive moderating effect on strengthening the effect of percentage of foreign shareholdings on the efficiency of the acquired local banks. In conclusion, concentration of foreign shareholdings and its country of origin are two factors that cannot be separated in affecting the level of efficiency of the acquired banks.

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