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Corporate Governance and Market Response: Mediating Role of Firm PerformanceEmpirical Evidence from Indonesia

Mohammad Iskak Elly[1], Grahita Chandrarin[2], Harmono[3]

[1,2,3] Doctoral Program, Economics, University of Merdeka Malang, Malang, Indonesia

ORCID ID: [2]http://orcid.org/0000-0002-7024-1315, [3]http://orcid.org/0000-0002-1933-5017

ABSTRACT: This research aims to investigate the influence of corporate governance on market response (R_{it}) through company performance (ROI). Corporate governance uses measurements of the intensity of participation of managerial ownership, independent board of commissioners, audit committee and institutional ownership in the process of monitoring the company's managerial processes. Using a quantitative approach with ordinary leasquare analysis techniques and path analysis. Data from 60 manufacturing companies with the observation period 2017 to 2021, totalingN 285 samples. The research results show that corporate governance variables are dominated by managerial ownership in influencing company performance (ROI) and the ROI variable partially mediates the relationship between managerial ownership of the company and stock returns. Meanwhile, independent commissioner ownership, audit committee and institutional ownership do not affect company performance or stock returns. Thus, the governance conditions of manufacturingcompanies in Indonesia are dominated by managerial ownership compared to the ownership of independent boards of commissioners, institutional ownership and audit committees. In other words, supervision of managerial process governance is only dominated by managerial ownership.

KEYWORDS: Ownership Structure, Firm Performance, Firm Value, IndonesiaGel Clasification: M21, M5.

1. INTRODUCTION

This research aims to analysis the influence of company ownership structure components on market response through company performance. In this case, company value is the company performance which is reflected through share trading activities on the capital market until the share market price is formed. Therefore, company value can be measured using the stock market price which can be denoted by several variable indicators including PER, PBV, Tobin's Q and stock return (pt-pt-1)/pt- 1, namely the current stock price t minus the t-share price t-1 divided by the stock price t-1 can reflect the market response (Harmono, 2023; Adi and Chandrarin, 2024). Further research Joecks, Pull and Scharfenkamp (2023), Examining corporate governance shows that gender-managed managers positively influence company value, this is in line with research (Mahrani and Soewarno, 2018; Tamrin *et al.*, 2017; Tumewu, 2014). Thus, several empirical corporate governance variables have been widely used to influence company performance. On the other hand, corporate governanceresearch can positively influence company value. This means that when the company managerial activity process is followed by good corporate governance, the market will respond positively (SiewYee, Sharoja Sapiei and Abdullah, 2018; Adi and Chandrarin, Grahita, Harmono, 2024) while corporate governance represented by foreign ownership can influence company value (Bokpin and Isshaq, 2009). Based on a series of research on corporate governance, its influence on company performance and company value shows that each component of corporate governance influences company performance in various ways. The difference in corporate governance component variables between countries varies in influencing company performance.

Therefore, this study re-examines the components of corporate governance which are proxied by managerial ownership, share ownership of the independent board of commissioners, audit committee, and institutional ownership for their influence on company value through company performance. In this case, company performance is observed for its role in mediating the relationship between corporate governance components and stock returns for empirical studies on manufacturing companies in Indonesia. On the other hand, ROI, ROA and ROE performance are often used as company performance variables that influence company value. In this case, the ROI obtained from earnings before interest and tax (EBIT) divided by total assets, will be compared withROA which is measured using net profit after tax (EAT) divided by total assets and its effect on stock return or company value.

(Nanda and Damayanti, 2021; Kurniati, 2019; Nugroho and Agustia, 2018).

Based on the background of the problem above, the discussion stages of this article chronologically include (1) background of the problem, followed by (2) literature review and development of research hypotheses, (3) research methods, (4) results and discussion of research results, and (5) conclusions and implications of research results.

2. LITERATURE REVIEW AND RESEARCH HYPOTHESIS

2.1. Corporate Governance and Firm Performance

Theoretically, this research is based on the theory of managerial behavior in relation to investors and creditors who act as principals, and the corporate governance parties involved which lead to upholding corporate governance values as agents, who are trusted to carry out the mandate given bythe principal to manage capital invested in order to achieve targeted profits, to maximize wealth for the principal. Thus, this research will discuss agency theory, of course supported by other related theories, including stakeholder theory and investment theory (Michael and Meckling*, 1976; Glambosky, Jory and Ngo, 2023). This research supports the principal agent theory of the first model, looking at the relationship between corporate governance values in terms of the company ownership structure consisting of managerial ownership, share ownership of the independent board of commissioners, audit committee, and institutional ownership, their influence on company performance which is generally measured using ROA, ROI, and ROE (Joecks, Pull and Scharfenkamp, 2023; Croci *et al.*, 2023; Noguera, 2020; Nguyen and Nguyen, 2020). Based on the underlying grand theory and several previous studies, the following research hypothesis can be formulated:

H_a1: Managerial ownership positively influences company performance

H_a2: Ownership of an independent board of commissioners positively influences companyperformance

H_a3: The audit committee influences company performance

H_a4: Institutional share ownership influences company performance

2.2. Firm Performance and Firm Value

Conceptually, company performance is fundamental performance which describes all the company performance related to the company managerial process activities, related to efforts to obtain revenue, management of costs and profits, as well as changes in the company financial position. Thus, this company performance often uses the measurement of profit before interest and tax divided by assets (ROI), profit after tax divided by assets (ROA), and profit after tax divided by equity (ROE). In this case, the final performance achievement is in the form of profit, and to determine the company overall performance, the profit obtained must be compared with the investment invested. Several studies that look at company performance use financial performance measurements (Susilo, 2022; Maditinos *et al.*, 2011; Mahrani and Soewarno, 2018). On the other hand, company value is a reflection of company performance which is reflected by share prices formed in the capital market mechanism. Thus, company value performance is the share market price in the capital market, which often uses measurements of price earnings per share (PER), return, price to book value (PBV), and Tobin's Q. Several previous studies have examined the influence of company performance on company value (Maditinos *et al.*, 2011; Kim, Kim and Lee, 2011; Siew Yee, Sharoja Sapiei and Abdullah, 2018; Harmono, 2023; Harmono *et al.*, 2023). Referring to a series of previous studies that observed the influence of company fundamental performance on company value, a research hypothesis can be formulated, namely:

H_a5: Company performance influences company value performance

2.3. Corporate Governance and Firm Value through Company Performance

Based on a sequence of previous studies, it is possible to trace the relationship between corporate governance components and company performance, and the influence of company performance on company value. A research model can be built on the influence of managerial ownership, ownershipof an independent board of commissioners, audit committee, and institutional share ownership on company value through company performance. (Kusuma and Nuswantara, 2021; Nanda and Damayanti, 2021; Kurniati, 2019; Nugroho and Agustia, 2018). The influence of share ownership structure on company performance in the manufacturing industry in various countries, including Europe, India and America, shows the consistency of research results, namely, there is monitoring of managerial processes, which is reflected by the role of the independent board of commissioners and the audit committee which can influence company performance (Choi, Lee and Park, 2013; Tanjung, 2020; Ben Fatma and Chouaibi, 2023; Edacherian *et al.*, 2023; Goto, 2009), Meanwhile, research in Indonesia shows that managerial ownership and institutional ownership influence company performance (Adi and Chandrarin, 2024) Therefore, there is a gap between the results of previous research, so this research will in an integrated manner examine the influence of corporate governance components on stock returns through ROI financial performance, an empirical study of manufacturing companies in Indonesia. In accordance with the conceptual framework built as a model, it can be outlined in Figure 1 Research Model as follows:

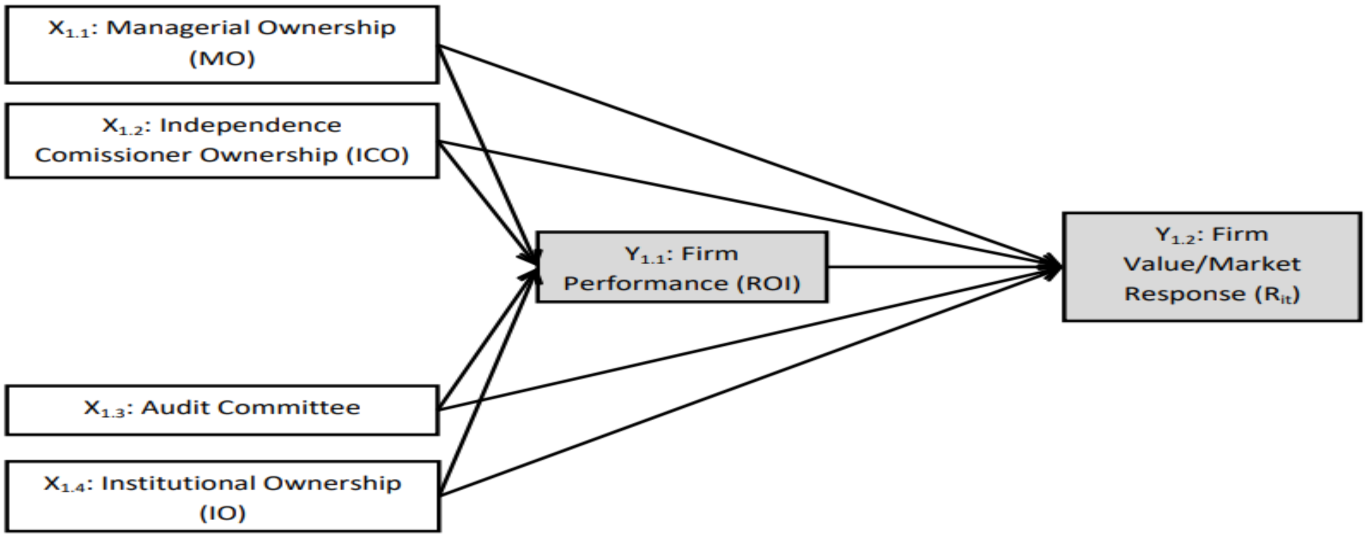

Figure 1: The Influence of Corporate Governance on Company Value Through CompanyPerformance

Referring to previous research and integrated research models, research hypotheses can beformulated:

H_a6: Managerial ownership influences company value performance through companyperformance

H_a7: Ownership of the Independent Board of Commissioners influences company value throughcompany performance

H_a8: The Audit Committee influences company value performance through companyperformance

H_a9: Institutional share ownership influences company value through company performance

3. RESEARCH METHODS

The research method uses a quantitative approach, in an integrated manner examining the influence of managerial ownership, ownership of an independent board of commissioners, audit committee, and institutional share ownership on stock returns through company performance (ROI). The research sample was 60 manufacturing companies with panel data observations for the period 2017–2021. N samples were 300. The analysis technique used path analysis, which was supported by multiple regression statistics. The detailed multiple regression analysis formula can be seen below:

$\{Y1.1ROIit \mid Y1.2Rit\} = \alpha + \beta1MOit + \beta2ICOit + \beta3ACit + \beta4IOit + eit$ equation (1)

$Y1.2Rit = \alpha + \beta1MOit + \beta2ICOit + \beta3ACit + \beta4IOit + Y1.1ROIit + eit$ equation (2)

Note:

$Y_{1.1}ROI_{it}$: Return on Investment $Y_{1.2}R_{it}$: Stock Return

MO_{it} : Managerial Ownership

ICO_{it} : Independence Commissioner Ownership AC_{it} : Audit Committee

IO_{it} : Institutional Ownership

e_{it} :error

4. RESULT AND DISCUSSION

4.1. Statistics Descriptive

Descriptive statistical results with N valid samples of 285 observations. The variable that has the highest average value is the managerial ownership variable of 3.017 with a low standard deviationof 0.798, the minimum value is 1. And the maximum is 5. Furthermore, the variable that has the second highest variation value is ROI company performance with an average value of 2.568 and standard The deviation above the average is 8,424, meaning that the diversity of data between companies is quite high with a minimum value reaching negative -0.467 and a maximum value of51,817. The next variable that has high data diversity is the company value variable (R_{it}) with an average value of 0.333 and a standard deviation of 1.070. On the other hand, the variation in data that is low below the average value is firstly the ownership of an independent board of commissioners with an average value of 0.944, and a standard deviation of 0.820, then the audit committee with an average of 1.635 and an average value of 1.316, and Lastly, institutional share ownership is relatively low with an average of 0.944 with a standard deviation of 0.271, a minimum value of 0.000 and a maximum value of 1.000. Detailed data description conditions canbe seen in Table 1.

Table 1: Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
MO	285	1.000	5.000	3.017	.798
ICO	285	.000	4.000	.944	.820
AC	285	.000	6.000	1.635	1.316
IO	285	.000	1.000	.668	.271
ROI	285	-.467	51.817	2.568	8.424
Rit	285	-1.000	4.273	.333	1.070
Valid N (listwise)	285				

Descriptively, the close relationship between variables shows that managerial ownership has a close relationship with ownership of the independent board of commissioners, audit committee and institutional ownership. On the other hand, managerial ownership has a negative relationship with company performance (ROI) and stock returns (Ri). In accordance with the concept of the audit committee's duties being responsible to the independent board of commissioners, it shows a positive relationship between the audit committee and the independent commissioners, thereby supporting the theory of corporate governance. The results of the next analysis show that company performance has a positive relationship with company value (Ri), this is consistent with previous research, investors will act rationally, when the company's performance is in good condition, the market will respond positively (Liow, 2010; Harmono *et al.*, 2023b; Croci *et al.*, 2023). In detail the relationship between variables can be seen in Table 2.

Table 2: Interrelationship between variables

	MO	ICO	AC	IO	ROI	Rit
MO	***1****					
ICO	***.330*****	***1****				
AC	***.164*****	***.271*****	***1****			
IO	***.157*****	.035	-.093	***1****		
ROI	***-.264*****	-.036	-.070	-.081	***1****	
Rit	***-.155*****	-.025	.009	.006	***.247*****	***1****

***. **. * Correlation is significant at the 0.01, 0.05, 0.10 level (2-tailed).

4.2. Results

Based on the results of research hypothesis testing, it shows a unique phenomenon in corporate governance. In this case, the role of management influencing company performance shows a negative regression coefficient of -0.271 with a probability value of (p=0.000). Thisphenomenon indicates that there is a managerial process effort to carry out earnings management which can reduce company performance (ROI). The supporting argument is that the company managerial behavior was also responded negatively by the market with a regression coefficient of -
0.112 (p=0.081). The role of ownership structure is an important factor that must be considered in improving company performance in line with research (Choi, Lee and Park, 2013; Tanjung, 2020). The results of this research differ from research in Europe where the results showed that gender diversity and CEOs had a positive influence on company performance (Ben Fatma and Chouaibi, 2023)

The condition of supervision by an independent board of commissioners influences company performance, showing an insignificant regression coefficient of 0.068 (p=0.278). Such conditions indicate that there is no good monitoring process for the governance of manufacturing companies in Indonesia. The course of the company's managerial process is more controlled by managerial ownership, which on average has the highest level of participation compared to the independent board of commissioners.

The role of the audit committee in supervising the company managerial process also shows that it does not affect the company performance, with a regression coefficient of -0.048 with a probability value (p=0.423), this also happens that the supervisory role of the audit committee isalso not responded to by investors in the capital market, it can be seen The role of the audit committee does not influence market returns with a regression coefficient of 0.045 and a probabilityvalue of (p=0.454), thus the company managerial process is still dominated by managerial ownership. This result contradicts the results of research in India which shows that the role of the audit committee can improve monitoring of managerial processes and can improve company performance (Edacherian *et al.*, 2023)

Finally, the role of institutional share ownership also cannot influence company performance with a regression coefficient of -0.045 with a probability value of (p=0.439). At the same time, the role of institutional ownership in influencing the process of determining managerial policies in general shareholder meetings has also not been responded to by investors in the market. capital. This can be shown that institutional ownership does not affect stock returns with a regression coefficient of 0.045 and a probability value of (p=0.441). Thus, it can be concluded that the condition of supervision of manufacturing company governance in Indonesia is dominated by managerial ownership. The results of this research are different from American conditions, when deregulation regarding company ownership structure is implemented it can increase the efficiencyof company performance. Thus, compared to conditions in various countries, the Indonesian government needs to pay close attention and carry out deregulation related to company ownership structures in order to improve corporate governance and increase the productivity of company performance (Goto, 2009)

Finnally, the role of mediating variables on company performance on the relationshipbetween managerial ownership, ownership of the independent board of commissioners, audit committee and institutional ownership with market response. ROI company performance is only able to mediate the relationship between managerial ownership and market response (R_{it}). Based on the results of the analysis of the relationship pattern between share ownership structure variables consisting of managerial ownership, ownership of the independent board of commissioners, audit committee and institutional ownership with market response through company performance (ROI), it shows that company performance is only able to partially mediate the relationship between managerial ownership and market response. By considering empirical results in Indonesia comparedto research results in several countries such as India, Europe, America, it seems that Indonesia needs to pay more attention to the condition of corporate governance and enforce regulations that can improve corporate governance monitoring mechanisms in order to increase efficiency and effectiveness of firm performance supported by good governance (Choi, Lee and Park, 2013;Tanjung, 2020; Ben Fatma and Chouaibi, 2023; Edacherian *et al.*, 2023; Goto, 2009). In detail, the phenomenon of corporate governance in inferential statistics can be shown in Table 3.

Table 3: Research Result

	Variable Definition	**Firm Performance ($Y_{1.1}$: ROI)**	**Market Response ($Y_{1.2}$:R_{it})**	**IndirectEffect**
$X_{1.1}$: MO	Managerial Ownership = $\frac{\%\ Managerial\ ownership}{Outstanding\ shares}$	**-0.271 (0.000)***	**-0.112 (0.081)***	**-0.061** (Partial mediation)
$X_{1.2}$: ICO	Independent Commissioner Ownership = $\frac{\%\ Independent\ Commissioner\ Ownership}{Outstanding\ shares}$	0.068 (0.278)	0.007 (0.916)	NS
$X_{1.3}$: AC	Audit Committee= Frequency of audit meetings within 1 year	-0.048 (0.423)	0.045 (0.454)	NS
$X_{1.4}$: IO	Institutional Ownership = $\frac{\%\ Institutional\ Ownership}{Outstanding\ shares}$	-0.045 (0.439)	0.045 (0.441)	NS
$Y_{1.1}$: ROI	Return on Investment = Institutional-Ownership =		**0.225 (0.000)***	NS

$\frac{Earnings\ After\ Tax}{debt+Equity}$			
Constant		**11.994 (0.000)*** **	**0.526 (0.070)***
Udj-R Square		**0.063 (0.000)*** **	**0.057 (0.001)*** **

5. CONCLUSIONS AND IMPLICATIONS OF RESEARCH RESULTS

5.1. Kesimpulan

The conclusion of the research results regarding the condition of manufacturing company governance in Indonesia in terms of the company ownership structure in relation to market response through company performance variables shows a unique phenomenon, namely, the dominance ofthe company's managerial process policy determination is dominated by the managerial ownership structure. This shows that the role of the mediating variable on company performance is only ableto mediate the relationship between managerial ownership and the stock return variable which reflects market response.

Ownership of an independent board of commissioners, audit committee, and institutional ownership do not show a significant role in the process of determining managerial policy, as shown by the influence of ownership structure on company performance, showing insignificant results, andalso not being responded to by the market.

5.2. Implications of research results

For the development of corporate governance theory, the results of this research can provideempirical evidence, the condition of corporate governance for the manufacturing industry in Indonesia is still not a monitoring process towards good corporate governance, therefore, further variation is needed for subsequent research and/or comparative socialization. with previous researchto produce more valid dissemination

For regulators. The results of this empirical study are important information, which can be used as abasis for ongoing evaluation and development in the context of improving regulatory determination in relation to corporate governance enforcement in Indonesia.

Harmono Harmono is a corresponding author, and an Associate Professor as a Lecturer and SeniorResearcher in Economics, Financial Management, and Capital Market at the University of Merdeka Malang, Indonesia. Contribute to data analysis, conceptual framework, and writing articles. He is also a Reviewer of the Journal of Intellectual Capital. Reviewer of Expertise Journal of Finance andBanking.

Mohammad Iskak Elly is a Mohammad Iskak Elly is a Doctoral Program, Economics, University of Merdeka Malang, Malang, Indonesia, He is also a Lecturer at Panca Marga University Probolinggo, as a senior Researcher in Capital Market Research and Financial Management

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APPENDIX

Definitions of Variables

ROI	*Return on Investment* is the ability of a company to make a profit compared to investment, thus focusing its attention on the operating assets, working capital and fixed assets.
IBCO	*Independent Board of Commissioners Ownership* describes the extentto which the ownership structure of shares is controlled in the contextof controlling voting rights in the direction of determining company management policies
ACO	*Audit Committee Ownership* is a capital ownership structure by the audit committee, whose job is to assist the Designers of Independent Commissioners and work closely with internal auditors
IO	*Institutional Ownership* representing many investors to invest inshares, including non-bank financial institutions, pension fund insurance, foundations, WAQF bodies, and other non-financialinstitutions
Firm Value	*Firm Value* is a concept of company value that is reflected by stockprices as a result of the demand and supply in stock trading transactions in the capital market
Market response (Rit)	Market reaction is a reflection of the response of investors in the capital market resulting from information on events related to companyperformance
GCG	*Good Corporate Governance* is the company's organizational values related to the value of transparency, organizational participation, agreement on the rules of the game, and accountability, which are generally measured through a share ownership structure. It is greatlyinfluenced by a country's economic system, including the capitalist economic system, socialist, and popular economy
Ownership Structure	*Capital Ownership Structure* consists of Independent Board of Commissioners Ownership, Managerial Ownership, Government Board Ownership, Institutional Ownership, Individual Ownership, Audit Committee Ownership, and Ultimat Ownership
Optimum Capital Structure	*Optimum Capital Structure* can occur when the condition of the economy is stable, the weighted average between the cost of debt capital and the cost of capital itself is at an optimal point due to theprocess of balancing through the market mechanism between the capital market and the debt funding market
Agency Theory	*Agency Theory* is a theory that explains the relationship between the principal and agent in this case, as the principal is the owner of the capital or investor and creditor, while the agent is the management of the company, the principal's relationship with the agent can empiricallyachieve optimal capital structure conditions
Corporate Governance	is a company's effort to create a pattern of conducive relationships between stakeholders in realizing company performance, which in turn supports increasing corporate value.