



Financial Risk and Capital Structure: Does it Contribute to Increasing the Company Value of Islamic Banking?

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Abstract:

This study aimed to determine the effect of financial risk and capital structure on the company value of Islamic commercial banks in 2016-2020. This research uses a quantitative method with a descriptive statistical approach. This research used panel data with analysis tools in panel data regression by Eviews. The sample in this study amounted to 11 Islamic commercial banks with a purposive sampling technique. Purposive sampling aims to obtain samples with specific criteria and follow the research objectives. The results of this study indicate that partially financial risk (NPF) and capital structure (DER) have no effect on company value, and financial risk (FDR) harms company value. Meanwhile, financial risk and capital structure simultaneously affect company value.

Keywords: Financial Risk, Capital Structure, Company Value

JEL Classification Code: D24, G21, G32

1. Introduction

In maximizing the value of their companies, Islamic banks cannot be separated from the risks faced. Financial risk is one factor that affects the company's value. External and internal companies are factors that affect financial risk. The bank's financial ratio factor can be an internal or internal factor of the company. At the same time, the country's macroeconomic situation becomes an external or external factor for the company (Somantri & Sukmana, 2019). Financial risks often experienced by Islamic banks are financing risk calculated through Non-Performing Financing (NPF) and liquidity risk calculated through the Financing Deposit Ratio (FDR). Islamic banks usually experience NPF risk in the financing sector, which is distributed to the public from deposits so that it can have an impact on company value (Pravasanti, 2017). Then FDR's risk is the distribution of Third-Party Funds (DPK) by Islamic banks for maximum financing. FDR is the ratio of the overall structure of the financing to be distributed to the general funds from the community and the capital utilized. Financial risk is significant to be applied to Islamic banks because there is a strong relationship with the company's overall risk and as a benchmark for managers in making financing distribution policies to customers (Yasin, 2019). Another study also said that financial risk is essential because financing distribution is a very fraught activity with consequences, so it needs correct policy in asset distribution (Herring & Schuermann, 2005).



Based on Islamic Banking statistics data from the Financial Services Authority (OJK), NPF and FDR growth from 2016 to 2020 experienced an increase, and a decrease in NPF was relatively stable compared to FDR's movement. In 2016-2018, it was seen that FDR's ratio experienced a growth of 6.52%, which means that Islamic banks in that year allocated too many funds to financing, and in 2018-2020 FDR experienced a slump of 7.21%. This condition is the same as the research that states that if the FDR ratio is high, it states that funds from third parties are more allocated to financing (Somantri & Sukmana, 2019). Likewise, the NPF value in 2017-2020 was 0.9% or increased so it can be concluded in the last 4 years. There is still an increase in non-performing financing in Islamic banks because it is too easy to provide loans due to demands in excess liquidity (Arifianto & Chabachib, 2016). A study stated that the financial risk variables measured through NPF and FDR were only FDR that influenced company value. At the same time, NPF did not experience a relevant impact on company value (Repi et al., 2016). However, other research states that FDR does not have a relevant impact on company value, but NPF has a positive and relevant impact on company value (Pravasanti, 2017).

One of the components that can result in good company value is the capital structure with a Debt-to-Equity Ratio (DER) as a proxy. This ratio can be calculated by dividing the total debt by the total equity (Nursyamsu, 2016). Financial managers have an essential role in managing the company's capital structure to create good corporate capital (Husnan, 2015). If the company's capital is good, the financial manager can manage his capital well. The capital structure can be a benchmark in knowing the role of financial managers in managing funds. Capital structure is the financial structure of a company whose use of funds is long-term to create a permanent source of funds so that it can affect the company's value (Fitria, 2021). In addition, the long-term debt of Islamic banks is in the form of bond and mortgage loans. The positive influence of using this debt is that it can help the capital turnover of Islamic banks within more than 1 year (Yani, 2016). However, the negative influence on Islamic banks is that Islamic companies or banks are difficult to make a profit and cannot pay off their debts.

The high ratio of bank DER shows that the bank's capital structure uses much debt, causing significant risks. The large portion of bank debt will make it difficult for banks to obtain profitability. A good bank capital structure should not exceed the enterprise's capital. So financial decisions are significant to reduce capital costs to increase company value. Companies whose capital is still experiencing a shortage can consider outside-sourced funding or debt (Brigham, 2015). However, companies must be selective in choosing funding from outside and efficiently optimize the capital structure (Nursyamsu, 2016). The capital structure variables measured through DER positively impact the Islamic Commercial Banks (BUS) company's value (Fitria, 2021). Other studies have



resulted in variable capital structure, and there is a negative and irrelevant impact on the value of Islamic commercial bank companies.

Companies that manage financial risk and have a sound capital structure can increase their company value. A stable company is a company that can increase the internal and external economic value of its company so that the value of the company is closely related to the high low price of shares traded in capital market instruments. The company's value becomes a valuable aspect for investors to make decisions in putting some of their funds into the company. The better and better the value of a company, the more investor loyalty to the company will increase (Adillah, 2020). Until now, Islamic banks provide loyalty by consistently publishing financial statements every period to make it easier and provide information to investors or the broader community in determining future decisions.

Companies or banks must pay attention to their financial risk ratio because high ratios such as NPF cause companies to experience problematic financing. The financing funds cannot be appropriately maximized, and the company's plans will experience obstacles (Yasin, 2019). Previous research that supports this was carried out by (Rasyidin, 2016) stated that the financial risk results proxied by NPF and FDR positively affected the company's value. A good and effective capital structure will later minimize capital costs so that the company's value can increase. Previous research that supports this was carried out by (Fitria, 2021) stated that the capital structure has a positive and significant effect on the company's value.

In this study, to determine whether a company's value is good, it is measured using economic value added (EVA). The measuring instrument invests an assessment of a company. If a positive EVA value is obtained, it means that the management is successful in increasing the value of the company. The EVA concept results in the company focusing on the capital structure and its calculation of economic profit with its measurement in a certain period so that an increase in the company's shares is created if the management performance is effective (Marshella & Hasanah, 2018). The EVA concept, which is more familiar with investors' piker patterns, can help a company's management. Based on the explanation above, researchers are interested in re-examining the "Effect of Financial Risk and Capital Structure on Company Value in Islamic Commercial Banks in Indonesia".

2. Literature Review

Banks in their financing rely on external parties and have the potential to have high risks compared to banks that use their funds whose results are internal (Somantri & Sukmana, 2019). Financial risks that Islamic banks often experience is financing risk (NPF) and liquidity risk (FDR), so it becomes a reference for the company's manager to control these risks to attract investors to invest their funds



in the company (Yani, 2016). According to (Somantri & Sukmana, 2019), FDR's risk is how much third-party funds (DPK) from Islamic banks are channeled for financing. FDR's high ratio indicates the bank's reasonable ability to manage its function as intermediation optimally and vice versa. However, too high this ratio makes the bank's liquidity decrease because more funds in the bank are allocated to financing, and vice versa, the lower this ratio indicates that the bank is liquid. In general, if the bank is increasingly liquid, there are many idle funds, so the intermediation function is not achieved. Therefore, company managers need to optimize financing disbursements to maintain bank liquidity (Akbar, 2020).

The company has a source of funds, one of which is its capital, so it is less necessary to consider outside funding such as debt when fulfilling the source of funds. According to (Fitria, 2021), if the company chooses debt to help the bank's operations, it must be careful and look for efficient funding because efficient funding can be seen from the optimal capital structure. The role of financial managers in managing capital is critical because the purpose of the company's capital structure is to reflect permanent sources of funds so that it can affect the company's value (Yani, 2016). The high DER ratio of banks indicates that the use of debt by banks is more significant, so that banks will have a considerable risk as well. In essence, companies whose debt is more petite than capital and debt guarantees for creditors in the form of good capital in their operations are successful in controlling and regulating company capital and debt.

Permana & Rahyuda (2019) defines that the better the company's value will increase the prosperity of the company owner so that the company's value is significant, so that later if the company is to be sold, it will be of high value. Another research from (Sujoko, 2007) suggests that a company's success in maintaining investors and investing in a company is the value of a company. Investors are more confident to invest in banks by looking at high company value because companies or banks must or are required to increase the value of their companies. According to (Adillah, 2020), the increase in company value becomes an achievement for the company. It becomes an obligation of managers who have been given the mandate to provide trust to the community and prosper the company owners. This study used a measuring instrument, namely EVA. The company's value can be valued by this method in terms of investment. Therefore, the positive EVA can prove that company management can increase the company's value and vice versa. A negative EVA shows a decrease in the company's value (Huda et al., 2019).

3. Research Methods

This quantitative research uses secondary data from BUS financial statements recorded on the OJK website for 2016-2020 by involving financial risks and capital structure proxied by NPF, FDR, and DER variables against the Company value represented by the following EVA variables.

Table 1: Operational Variables

| Variables | Symbol | Description | Data sources |
|----------------------------|--------|--|--------------|
| <i>Exogenous Variables</i> | | | |
| Non-Performing Financing | NPF | The risks experienced by banks because their customers default | OJK |
| Financing Deposit Ratio | FDR | Ratio of funds third parties channeled to financing on Islamic banks | OJK |
| Debt-to-Equity Ratio | DER | Financial ratio comparing the amount of debt to equity | OJK |
| <i>Endogenous variable</i> | | | |
| Economic Value Added | EVA | Difference in operating profit after tax | OJK |

The population in this study was taken and determined from the BUS, officially recorded at the OJK in 2016-2020 as many as 14 BUS. Researchers used purposive sampling to determine the samples used in this study. Researchers obtained 11 BUS samples. This research was assisted by Eviews 10 software and used the regression analysis method. Regression of panel data with estimation model determination to select the best model among common, fixed, and random effects through Chow, Housman, and Lagrange multiplier tests. In addition, this study also conducted a descriptive statistical analysis, determining the influence partially (t-test), simultaneously (f-test), and the value of the coefficient of determination based on the relationship in the model.

4. Finding and Discussion

Descriptive statistical analysis is a test to analyze and interpret numbers or data on each variable studied, which aims to explain the picture related to events or circumstances (Rukajat, 2018). The benefit of this analysis is to make it easier to categorize data results by a group to make it easier to interpret.

Table 2: Descriptive Statistics of Variables

| Indicator | NPF | FDR | DER | EVA |
|-----------|----------|----------|----------|-----------|
| Mean | 2.935091 | 87.25182 | 2.049976 | -4.29E+10 |
| Maximum | 22.04000 | 196.7300 | 6.230000 | 2.70E+12 |
| Minimum | 0.010000 | 63.94000 | 0.380000 | -2.75E+12 |
| Std. Dev. | 3.770762 | 18.00634 | 1.411432 | 6.07E+11 |

Source: Eviews data processed

Descriptive statistics show that the minimum value on NPF is 0.01, namely BCA Syariah in 2020, while the maximum value is 22.04 at BJB Syariah in 2017. It shows that there is still problematic financing in one of the Islamic banks, NPF on BJB Syariah, which exceeded 5% in 2017. In addition, the average NPF

value in Islamic banks reached 3.77, meaning that overall co-financing is still well controlled. Then, FDR's value shows a minimum value of 63.94 contained in Bank Mega Syariah in 2020, and then the maximum value is 196.73, which is contained in Bukopin Syariah in 2020. It shows that FDR's value ranges from 63.94 to 196.73, which means that the management of deposits in Bukopin Syariah in 2020 is not good because it is not following bank Indonesia's limit of 100.00 and needs special attention to the bank. Similarly, the mean value of FDR was 87.25, more significant than the Std. Dev value of 18.00. So, FDR has a small distribution of data.

Furthermore, the DER value showed a minimum number of 0.38 at Bank BCA Syariah in 2016, then a maximum value of 6.23, found in Bank Victoria Syariah in 2019. It shows that the DER value ranges from 0.38 to 6.23 and means that Islamic commercial banks can still maintain their liquidity levels. Then, the EVA shows the minimum and maximum values of -2.75 and 2.70 contained in Bukopin Syariah in 2017 and BNI Syariah in 2016. Then, the estimation model determination results showed that the best model in this study was in the form of Random Effect, so the test was referred to in the panel regression analysis as follows.

Table 3: Panel Data Regression of Random effect

| Variables | Coefficient | Std. Error | t-statistics | Prob. | R-square | Prob. f-statistics |
|-----------|-------------|------------|--------------|---------|----------|--------------------|
| C | 1.15E+12 | 4.36E+11 | 2.641074 | 0.0109 | 0.165478 | 0.025394* |
| NPF | 2.74E+09 | 2.27E+10 | 0.120434 | 0.9046 | | |
| FDR | -1.38E+10 | 4.76E+09 | -2.900319 | 0.0055* | | |
| DER | 6.05E+08 | 5.99E+10 | 0.010097 | 0.9920 | | |

Note: *Significant at 0.05

Source: Eviews data processed

The results of the t-test showed that only the FDR variable had a significant influence on EVA with a probability value of 0.0055 or < 0.005 with a coefficient value of -1.38E+10. It means that if FDR, an Islamic bank, increases by 1, it will reduce the company's value by 1.38. (Ebenezer et al., 2019) said that the higher the FDR ratio of a bank would reflect the more ineffective it is financing distribution, so this ratio must remain within limits set by Bank Indonesia. Bank Indonesia sets limits to create effective financing disbursements, which is expected to increase bank income (Syakhrun et al., 2019). Then, the results of f test and the coefficient of determination showed a significant influence on the relationship between exogenous variables to endogenous based on a probability of 0.025394 or < 0.005 and an R-square value of 0.165478. It means that the company's assessment needs to involve capital and financial risks because it can be used as a benchmark for company management in seeing the company's value and as material for company evaluation (Karamoy et al., 2016). In addition, it can be concluded that the NPF, FDR, and DER variables can explain their effect by



16.54% on EVA, while other factors outside the research model explain the remaining 83.46.

5. Conclusions

This study aims to measure the influence between the influence of NPF, FDR, and DER on EVA on Islamic Commercial Banks partially and simultaneously. The test results on the t-test showed that only the FDR variable had a significant negative influence on EVA. In addition, Variabel FDR has a negative influence on the value of the company on BUS. However, the variable NPF and capital structure do not influence the value of Islamic banks. Meanwhile, the results of the f test showed a significant influence simultaneously with a coefficient of determination value of 16.54% on EVA. It means that there are still variables outside the model that can affect the value of EVA but have not been involved in this study, so subsequent studies can add other variables as a measuring tool to evaluate Islamic banks. In addition, it can also add more comprehensive search objects such as Islamic banks categorized as BUS and Islamic Rural Banks (BPRS) with a longer time frame to get more complete results. Islamic banks pay more attention to and consider the distribution of financing funds so that they can develop in the future, but by paying attention to the limits that have been determined by Bank Indonesia so that later with a good FDR can increase profits for banks.

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