Risk Management Disclosure And Their Effects On Banking Firms Value In Indonesia

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RISK MANAGEMENT DISCLOSURE AND THEIR EFFECTS ON BANKING FIRMS VALUE IN INDONESIA

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ABSTRACT

Risk management is some effort done to minimize the possible risks that might occur in the future. This study aims to examine the influence of firm size, audit committee, and risk committee on risk management disclosure and to examine the influence of firm size, audit committee, risk committee, and risk management disclosure on firm value. The research sample is 40 banking firms listed on the Indonesia Stock Exchange (IDX) during 2016 to 2018. The hypothesis testing was done by using regression of data panel. The results reveal that the firm size and risk committee have a positive influence on the disclosure of risk management, audit committee does not have a positive influence on the disclosure of risk management. This study has also unsuccesfully proved the positive influence of firm size, audit committee, and risk committee on firm value through risk management disclosure. The limitation of this study is that the measurement of the risk management disclosure index contains an element of subjectivity in understanding the index, so it has the opportunity to give different perceptions if research is carried out in the future. The implication of this study can be to consider the size of the company and the risk committee, so that it will minimize the risk for investors.

Contribution/Originality: This study investigates the measurement of the risk management disclosure index on the Indonesia Stock Exchange (IDX) based on agency and stakeholder theory. The study examines four main variables (company size, audit committee, risk committee, and voluntary risk management disclosure) to understand whether they affect risk management disclosure and firm value that are interesting to study.

1. INTRODUCTION

The regulation of The Finance Services Authority No. 18/POJK.03/2016 article 30 on The Application of Risk Management for Commecial Banks, states that banks are required to disclose risk management in their annual published reports with minimum disclosures covering the performance of risk management and the direction of risk management policies (Financial Services Authority/ OJK, 2016) . The obligation to disclose risk management in banking is closely related to the nature of the banking industry which is full of activities that contain risks, including advancing funds to customers, collecting funds from customers, selling, buying, and quaranteeing the risk itself. A survey conducted by Center for Risk Management Studies (2018) revealed that there are a few risks a company encounters, one of which is the main one is the risk of changing company direction. Therefore, banks should be able to handle risks by applying risk management. Such application is not merely for the management's interest, but also for customers related to product information and the banks' activities.

Prior studies have been found regarding the factors that influence the disclosure of risk management. Gunawan and Zakiyah (2017) and Elfeky (2017) found that firm size could be the factor affecting risk management disclosure. Khumairoh and Agustina (2017) and Muslih and Mulyaningtyas (2019) revealed that firm size does not have an effect, so that it could not be the factor affecting risk management disclosure. Al-Maghzom, Hussainey, and Aly (2016) stated that a number of audit committte meetings had an influence on risk management disclosure. Setiany, Hartoko, Suhardjanto, and Honggowati (2017) found that the frequency of audit committee meetings did not influence risk management disclosure, so that it could not be the factor affecting risk management disclosure. Abdullah and Ismail (2015) stated that a number of committee meetings, risk, and firm size had an influence on hedging disclosure which contains elements of mandatory and voluntary disclosure. This study used a sample of 300 companies listed on the Malaysian Stock Exchange in 2013. Given that prior reseach findings that are still inconsistent, this current research aims to reexamine risk management disclosure using the financial statements of banking industry as the research object. The companies being investigated were listed on the IDX during the period 2016 to 2018. Selecting banking industry is based on the notion that it is one of finance industries which is growing fast in the digital era.

2. THEORETICAL BACKGROUND OF THE RESEARCH

2.1. Agency Theory

The separation of ownership and control may result in conflicts between principal and agent (Ghosh, 2018). In this case, the principal considers the agent unable to run a company by ignoring the principal's interests (Zogning, 2017) . In contrast, the agent thinks that the one who fully understands and can run a business is the agent itself. Agency theory comes into existence due to diverse individuals' purposes to gain their best interests in an organization they are involved. Managers run a company in a sovereign way and are supported by their managerial competence. Nevertheless, they are the agent appointed by the principal to delegate the authority.

The disclosure of risk management is expected to minimize asymmetric information and provides good opportunities for investors in terms of the effectivity of decision-making and assessing a company's viability in the future. Risk information can help the principal monitor the management effectivity in dealing with problems. The risk information revealed is more likely to decrease asymmetric information and build investors' trust thus increasing market valuation (Bravo, 2017).

2.2. Stakeholder Theory

According to Freeman and David (1983) a company has a responsibility to its stakeholders, including shareholders, employees, customers, suppliers, lenders, and society. All stakeholders own the right to be informed about the company's activities carried out by the executives. Disclosing risk management is one of corporate strategies to have a relationship with stakeholders. It is also a strategic management process in calculating business problems the company comes across. So, in this case, the company is encouraged by its stakeholders to disclose more information than needed to meet the information challenges nowadays (Elfeky, 2017). The more in depth and broader the disclosure, it shows that the company intends to meet the stakeholders' information needs.

2.3. Risk Management Disclosure

Risk is potential loss due to the occurrence of an event. The Financial Services Authority stated that there are eight types of risks a company encounters – credit risk, market risk, liquidity risk, operational risk, compliance risk, legal risk, reputation risk, and strategic risk. Risk itself is closely related to uncertainty. Things that are uncertain will be more likely to cause risks. Therefore, it is important to manage risks in order that the expected results can be achieved. Risk management is a series of methodologies and procedures used to identify, measure, monitor, and control risks that possibly rise in the entire business activities of a bank.

Based on the National Survey of Risk Management conducted by Center for Risk Management Studies (2018) the implementation of risk management is useful for (1) improving employee performance, (2) improving job satisfaction, (3) efficiency of resource uses, (4) improving effectiveness and efficiency of supply chain, (5) improving customer satisfaction, (6) improving service quality.

2.4. Research Hypotheses

Each firm has a different size. The larger the firm size, the broader the information disclosed. This means a larger firm does more disclosure due to pressures from various parties. This statement is strengthened by studies of Elfeky (2017) and Yunifa and Juliarto (2017) revealing that firm size had an influence on risk management disclosure. Based on the explanation, H1 is proposed as follows: Firm size has a positive influence on risk management disclosure.

Based on the Regulation of Bank Indonesia No 14/14/PBI/2012 regarding Transparency and Publication of Bank Report in creating market discipline to be aligned with developments in international standards, it is necessary to increase the transparency of the financial condition and performance of banks by publishing reports to make it easy for public and market players to do assessments (PBI No. 14/14, 2012) . To that end, audit committee serves to ensure that the financial statements prepared are presented fairly in accordance with accounting principles and are protected from possible risks. The frequency of audit committee meetings plays such an important role for the effectivity of audit committee. The more frequently the audit committee holds meetings, the better the supervisions of the bank so as to provide good quality information. This statement has been proven by studies ofAl-Maghzom et al. (2016) and Alkurdi, Hussainey, Tahat, and Aladwan (2019) revealing that audit committee meetings had an influence on risk management disclosure. The explanation leads to H2 proposed as follows: Audit committee has a positive influence on risk management disclosure.

Beside audit committee, there is a risk committee. It serves to provide the real description of the risks and disclosing the risks faced by a company. The effectivity of a risk committee in carrying out its functions is reflected in the number of meetings held. Through risk committee meetings, information disclosure can be deeper and wider. This statement is supported by studies of Abdallah, Hassan, and McClelland (2015) and Bello, Yusuf, and Nuhu (2019) revealing that the frequency of risk committee meetings had an influence on risk management disclosure. H3 is then proposed as follows: Risk committee has a positive influence on risk management disclosure.

Another aspect is total assets. Total assets can provide the size description of a firm. The larger the total assets of a firm, the larger the firm size. Furthermore, the larger the firm size, the more interested the investors in the firm (Raharja & Putra, 2016). Their interest in the firm will be more likely to affect the decision making process in buying its stock. The more investors who are interested in the firm's stock, the firm value will rise. This elaboration leads to the proposal of H4 is Firm size has a positive influence on firm value.

Audit committte is created by an independent commissioner to supervise the company performance. Independent audit committee is expected to be able to provide transparency of management accountability of financial statements. Supervising the company by the audit committee is more likely to attract stakeholders to invest in the company. To make an effective decision, a sufficient period of time and well-organized plan are required in a group, so that audit committee meetings can be a facility to achieve effective decision. The more frequently the audit committee holds meetings, the better the decisions will be made, thus increasing firm value. This statement has been proven by the study of Sarpal (2017). Based on this explanation, H5 is proposed as follows: Audit committee has a positive influence on firm value.

Given the complexity of risks faced by banking sector, the role of risk committee is highly needed and separated from audit committee. The risk committee set up strategies upon the risks being faced and deliver them to the stakeholders. The risk committee meetings being held will boost the acts of monitoring and risk reporting, thus reducing the negative impacts on firm value. This statement has been researched by Kakanda, Salim, and

Chandren (2018) who found that a number of risk committee meetings spurred better decision makings. This explanation leads to H6 proposed as follows: Risk committee has a postive influence on firm value.

Basically, risk disclosure can help investors make decisions related to a company's future. When the risks are diclosed in details, it will enhance the investors' interest which in turn rise the firm value in the market. Information disclosure can minimize information assymmetry and provide more complete information in order that investors can assess a firm well. This statement has been proven by studies of Abdullah, Ismail, and Isa (2015) and Bravo (2017) revealing that risk management disclosure had an influence on firm value. Thus, H7 is proposed as follows: Risk management disclosure has a positive influence on firm value.

3. METHODS OF THE RESEARCH

3.1. Research Sample

The population in this research is the banking industry's firms listed on the IDX during the period 2016 to 2018. Purposive sampling was used to select the research sample with a few criteria - the firms publish annual financial stataments, they are not delisted from the stock exchange during the research term, and have complete data related to the research variables. The number of reasearch sample is 40 firms with a total of 120 firms observed during three yea.

3.2. Research Variables

The dependent variable in this study is firm value; the independent variables are firm size, audit committee, and risk committee; the intervening variable is risk management disclosure. Firm size is the scale of determining the size of a firm. Firm size as the natural logarithm is measured from the book value of total assets in the given period. Firm valus is measured by using Tobin's Q based on the market value of equity added with the book value of liabilities, divided by the book value of total assets.

Audit committee is the committee created by and responsible to the commissioner board in assisting the board carry out its duties and functions. Audit committee is measured by the number of meetings held during one effective period in the firm.

Risk committee is the committee created by and responsible to the commissioner board in assisting the board monitor the implementation of risk management and assess the risk tolerance that might be taken by the firm. Risk committee is measured by the number of risk committee meetings held during one effective period in the firm.

Risk management disclosure is the disclosure of information by the management regarding the control of risks arising from the company's activities. It is measured using content analysis techniques with coding indices. The coding unit used in this analysis is indicated by the number 1 if the company discloses risk management, and 0 if the company does not disclose risk management. The indices of risk management disclosure consist of 45 disclosure items (Abdullah., Shukor, Mohamed, & Ahmad, 2015). The score of risk management is calculated from the amount of the disclosed and divided by the total indices of disclosure.

3.3. Data Analysis Method

This research study employs regression of panel data by selecting the right model to estimate the regression of panel data, namely Common Effect Model (CEM), Fixed Effect Model (FEM), and Random Effect Model (REM). Determining the most appropriate model is done by (1) Chow-Test to determine better estimation between common effect model or fixed effect model, (2) Hausman Test to determine if the model to be selected is random effect or fixed effect.

The hypothesis testing was conducted by using T test, with the regression model of panel data as follows:

Model 1

$$VMRD = \beta 0 + \beta 1SIZE + \beta 2ACM + \beta 3RCM + e1$$

Model 2

$FV = \beta 0 + \beta 1SIZE + \beta 2ACM + \beta 3RCM \beta 4VMRD + e2$

Notes:

$\beta 0$	= *Regression Coefficient of Constanta*
$\beta 1,2,3,4$	= *Regression Coefficient of each Proxy*
FV	= *Firm Value*
SIZE	= *Firm Size*
AC	= *Amount of Audit Committee*
RC	= *Amount of Risk Committee*
VMRD	= *Risk Management Disclosure*
e1,2	= *error*

4. RESEARCH FINDING AND DISCUSSION

4.1. Descriptive Statistics

The research sample is 40 firms with 120 observed data taken by using purposive sampling. The analysis of descriptive statistics can be seen in Table 1.

Table 1. Results of descriptive statistics.

Variables	n	Minimum	Maximum	Sum	Mean	Std. Dev.
FV	120	0.188	2.118	130.708	1.089	0.246
VRMD	120	0.440	0.840	82.220	0.685	0.083
SIZE	120	27.223	34.799	3732.284	31.102	1.861
ACM	120	3.000	32.000	1318.000	10.983	6.293
RCM	120	2.000	34.000	967.000	8.058	5.114

Source: Processed data, 2020.

4.2. Regression Analysis of Fixed Effect Model

The result of model testing using Chow test has yielded the prob 0.000 on Cross-section F, while the result of Hausman test for both models has gained the probability < 5%. Thus the model selected is the fixed effect.

The regression analysis of panel data of fixed effect model is conducted to find out the the influence of independent variable on dependent variable. The results of this regression provides constanta value and probability value of each independent variable, as seen in Table 2 and Table 3.

Table 2. Results of panel data regression (Fixed Effect Model) 1.

Dependent Variable: VRMD		
Variable	**Coefficient**	**Prob.**
C	-1.675	0.007
SIZE	0.076	0.000
ACM	-0.001	0.052
RCM	0.003	0.004

Source: processed data, 2020.

Table 3. Results of panel data regression (Fixed Effect Model) 2.

Dependent Variable: FV		
Variable	**Coefficient**	**Prob.**
C	11.722	0.000
SIZE	-0.328	0.002
ACM	0.004	0.237
RCM	-0.010	0.071
VRMD	-0.584	0.281

Source: processed data, 2020.

4.3. Model Testing

To test the feasibility of the regression model used, F test and determination test are conducted to examine the influence of independent variable on dependent variable. From the results test on model 1, it is known that the value of adjusted R-squared is 0.933455, while model 2 is adjusted R square 0.83048.

The F test on the regression of fixed effect model has yielded a probability of 0.000000. Such value is smaller than α 5% (0.000000 < 0.05). Thus, the regression model used in this research study is fit to use.

4.4. Results of Path Test

Path test aims to find out the direct and indirect effect of independent variable on dependent variable through intervening variable. The results are presented in Figure 2:

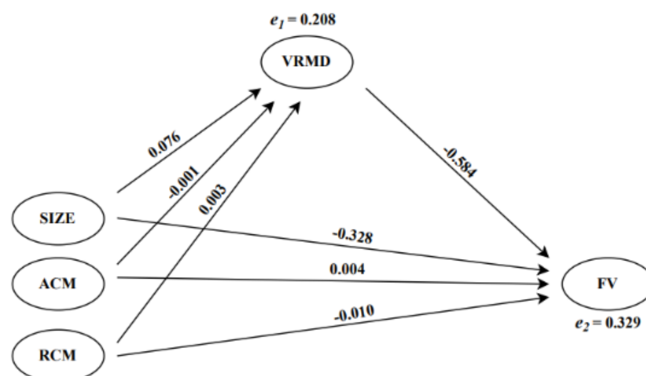

Figure 2. Results of path test.

Based on the results of the path test, the regression coefficient on the direct effect of size on firm value is smaller than the effect of size on firm value through risk management disclosure. The regression coefficient on the direct effect of audit committee on firm value is larger than the effect of audit committee on firm value through risk management disclosure. In the meantime, the regression coefficient on the direct effect of risk committee on firm value is smaller than the effect of risk committee on firm value through risk management disclosure.

To prove the significance of the indirect effect of the independent variables on the dependent variable, the Sobel test was carried out. Table 4 shows that risk management disclosure as the indirect effect is insignificant.

Table 4. Results of sobel test.

Information	p-value
SIZE→VMRD→ FV	0.296
ACM→VMRD→ FV	0.341
RCM→VMRD→ FV	0.308

Source: output data.

5. RESULTS OF HYPOTHESIS TESTING

Firm size measured by total assets has a coefficient value of 0.075521 and probability value of 0.0002 < 0.05. It indicates that firm size has a positive significant influence on risk management disclosure, which means H_1 is supported. This reseach finding explains that the larger the compay, the broader the disclosure of risk management. The positive relationship between firm size and VRMD might be caused by several things. First, larger-sized banks are able to disclose risk management broader compared with small-sized ones. Second, based on stakeholder theory, larger-sized banks have more stakeholders who are pressuring the management to make greater risk management disclosures so that the information disclosed is more complete and as a form of management accountability to the capital owners. Broader disclosures are more likely to boost investors' trust, as it has such an important role in a

firm. Larger-sized firms usually have good governance to support broader disclosures. This research finding – the supported hypothesis, is consistent with the research findings of Elfeky (2017); Gunawan and Zakiyah (2017) and Abdullah and Ismail (2015).

Audit committee (ACM) measured by the amount of audit committee meetings each year has a coefficient value of -0.001478 and probability value of 0.0515 < 0.05. It indicates that audit committee does not affect risk management dislosure, which means H_2 is not supported. This research finding has proven that the frequency of holding meetings by audit committee does not affect the extent of risk management disclosure. In this research study, the meeting activities do not show the effectiveness of monitoring process in banking. This occured might be due to ineffective quality of the meetings. This research finding – the rejected hypothesis, is in line with the research conducted by Sellami and Fendri (2017).

Risk committee (RCM) measured by the amount of risk committee meetings each year has a coefficient value of 0.003408 and probability value of 0.0040 < 0.05. It indicates that risk committee has a positive significant influence on risk management disclosure, which means H_3 is supported. This result explains that the more frequently the risk committee held meetings, it would affect the extent of risk managaement disclosure. The positive relationship between the risk committee and the risk management disclosure occurred due to a few things. First, the agenda of meetings held by the risk committee served as a forum for check-and-balance management activities and for reporting various problems and conflicts that arised. Second, the agenda of meetings by the risk committee served as the media to share information, knowledge, and expertise to provide quality information. As it is well-known that risk management disclosure functions to minimize the information asymmetry between the managers and investors, as well as to meet the information needs of the stakeholders. This research finding corroborates the research findings of Abdullah. et al. (2015) and Bello et al. (2019).

Firm size measured by total assets has a coefficient value of -0.327788 and probability value of 0.0016 < 0.05. It indicates that firm size has a negative significant influence on firm value, which means H_4 is not supported. When the management implement transparent disclosure of complex problems, it may cause misperceptions among shareholders. So, a firm chooses to restrict the scope of risk disclosure to avoid the decreasing investors' interests. This research finding supports the study of Onasis and Robin (2016).

Audit committee (ACM) measured by the amount of audit committee meetings each year has a coefficient value of 0.004312 and probability value of 0.2371 < 0.05. It indicates that audit committee does not influence firm value, which means H_5 is not supported. This is probably because the more frequently meetings are held, the more they will cost and it will repeat to produce similar decisions or easily change decisions. Thus, the research finding that shows a positive but insignificant direction indicates that the amount of audit committee meetings is not the relevant factor to measure firm value. This hypothesis result is consistent with the study of Olayinka (2019).

Risk committee (RCM) measured by the amount of risk committee meetings each year has a coefficient value of -0.010489 and probability value of 0.0709 < 0.05. Thus, H_6 is not supported. It means the more frequently the risk committee holds meetings, it will not affect firm value. This is likely because the investors more consider the external factors of the company. This research finding – the unsupported hypothesis is in line with Elamer and Benyazid (2018).

Risk management disclosure (VRMD) measured by the amount of indices of risk disclosure has a coefficient value of -0.584144 and probability value of 0.2812 < 0.05. This indicates that risk management disclosure does not affect firm value, which means H_7 is not supported. This result explains that broader disclosure of risk management does not affect firm value. This research finding is consistent with the studies of Al-Maghzom et al. (2016) and Anton (2018). The absence of influence of independent variables on firm value might be due to external factors that the investors more consider, such as interest rate, currency rate, political conditions.

6. CONCLUSIONS

Based on the research findings and discussions, a few conclusions can be drawn. First, firm size and risk committee have a positive influence on risk management disclosure. Second, all independent variables – firm size, audit committee, risk committee, and risk management disclosure do not influence the dependent variable, firm value. Third, risk management disclosure has been proven not to mediate firm size, audit committee, and risk committee on firm value.

This research study has succeeded in proving the stakeholder theory that a large number of stakeholders owned by larger-sized banks will encourage the banks to provide more information, including risk management disclosure. Larger firms disclosing risk management more broadly aims to avoid information asymmetry to occur.

In relation to limitations, there are few limitations in this study. The measurement of risk management disclosure indices contains subjectivity, so that people will possibly have different perceptions. Based on the research finding to minimize risks, investors may consider firm size and risk committee, because the larger the firm, the more frequently the committee holds meetings to encourage more risk management disclosure, thus minimizing risks for investors.

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