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The Effect of Intellectual Capital and Corporate Governance on The Performance of Village Credit Institutions

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ABSTRACT

The main purpose of this paper is to examine and analyze the effect of intellectual capital and corporate governance on the performance of village credit institutions in Tampaksiring District, Gianyar, Bali. The study population were 32 village credit institutions with 96 respondents. The findings show that there is a positive influence of intellectual capital and corporate governance on the performance of village credit institutions. This indicates that intellectual capital and good corporate governance of village credit institutions, such as human capital, capital structure and relational capital highly will improve the performance of village credit institutions.

Keywords: Corporate Governance, Intellectual Capital, Village Credit Institutions (LPD)

INTRODUCTION

Village Credit Institutions (LPD) are institutions owned by traditional villages in Bali, established in 1984 and pioneered by Bali Provincial Government. According to recent regulation (Bali Provincial Regulation No. 3 of 2017), Village Credit Institutions are to guarantee the realization of customary community welfare as members of customary villages. Since they provided economic, social and cultural benefits to the villagers, the institutions are worth improving as financial institutions owned by the customary village.

Since their establishment, the institutions have been exponentially flourishing both in numbers and in progressions. Until 2018, there have been 1,433 LPDs established in each customary village, to handsomely contribute to the village's economic development through the business profits they obtain. As savings and loan service providers, they continually grow following the goings-on of Balinese socio-economic and cultural dynamics.

As financial institutions, the LPDs must fight off intense business competition to get more customers with banks, and cooperatives. These competitors could reduce their customers in rural areas. Thus, the LPDs are required to be able to successfully compete and improve its performance to sustainably carry out their business.

To win the competition, LPDs' intellectual capital and corporate governance are their main assets. Intellectual capital is essential to improve institutional performance. According to Kartika and Hartane (2013) intellectual capital is the main asset of a company in addition to physical and financial assets. It occupies a vital role to manage physical and financial assets, to produce valuable products, to manage the organization and to establish relationships with external parties. These all undoubtedly require the ability and thinking power of employees as company’s intellectual assets. (2016), Lustyaningsih (2015), Simarmata (2015), Shofa (2014), and Syatia and Yushita (2017) provide empirical evidences that intellectual capital variables have a positive influence on financial performance. However, Harianja and Fauzie (2013) pointed distinct results as the research found that intellectual capital had a negative effect on company's financial performance. In addition, Arini (2018) argued that intellectual capital had no influence on company's financial performance.

Village Credit Institutions (LPDs) are separately managed with villagers to enable agency problem. To minimize them, good corporate governance is beneficial to bridge yawning gaps between agents and principals. Successful implementation of good corporate governance will effectively prevent mistakes in decision making and actions. Some research (e.g., Bulandari, 2015; Sandraningsih & Putri, 2015; Mahaendrayasa & Putri, 2017; and Setyawan & Putri, 2013) contended that good corporate governance variables have a positive influence on performance. This is in contrast with Takarini (2014) argued that good corporate governance has a negative effect on company's financial performance. Additionally, Nopiani, et al (2015), and Wijayanti (2012) found that good corporate governance had no influence on company's financial performance.

This study aims to examine and analyze the effect of intellectual capital and corporate governance on the LPDs performance. This study was conducted in Tampaksiring sub-district, Gianyar, Bali. Tampaksiring is one of tourism centers in Gianyar Regency, contributing to its rapid economic development which heavily influenced the significant development of those LPDs.

Agency relationship perspective is considered essential for better understanding of corporate governance. Jensen and Meckling (1976) stated that agency relationship is a contract between a manager (agency) and a shareholder (principal). The agency relationship sometimes creates problems between managers and shareholders since humans, as economic animals, have the nature of selfishness and self-interests. Shareholders and managers have different goals and each wants their goals to achieve resulting in a conflict of interest. Shareholders want greater and immediate returns on their investment while managers want their interests to be accommodated with maximum compensation or initiative for their performance in running the company. Siagian (2011: 11) stated that agency theory uses three basic assumptions. They are:

1. Humans in general are selfish.
2. Humans have limited thinking power about the perception of the future (bounded rationality), and
3. Humans always avoid risk (risk averse)

These assumptions explain why agency conflict occurs between managers and shareholders. Managers tend to prioritize their personal interests rather than the interests to increase the value of the company. With this opportunistic behavior, they act to achieve their own interests, whereas they should be in favor of shareholders’ interests because they are the ones who give the managers authority to run the company.

Corporate governance, which is a concept based on the agency theory, is expected to function as a tool to provide confidence to customary village manners and customers, enabling them to receive a return on funds they have invested. Suvanmanee, et al.

(2020) highlighted the significance of good corporate governance to avoid miscommunication in all company's segments and to realize a perfect organizational culture. Corporate governance relates to how customary villagers and customers believe that LPD managers will benefit them, believe that LPD managers will not defraud, embezzle or their fund, or invest in unrelated projects. In other words, corporate governance is expected to function to reduce agency costs.

Intellectual capital comprises intellectual material of knowledge, information, intellectual property rights, and experience used to create wealth. Pulic (2000) suggested three components of intellectual capitals, including human capital, which is a combination of knowledge, skills, creativeness, and individual abilities in a company.

Competent human capital could encourage increased financial performance. Khasanah (2016), and Syatia and Yushita (2017) found that intellectual capital has a positive influence on financial performance. This implies that the better the intellectual capital of a company or institution, the more increasing the performance of the company or institution. Based on this, this study puts forward the following hypothesis:

H1: Intellectual capital has a positive effect on the performance of Village Credit Institutions (LPDs)

In addition to intellectual capital, corporate governance is a management system designed to improve company performance, protect the interests of stakeholders and increase compliance with laws, regulations, and generally accepted ethical values. It is a set of rules governing relationships between shareholders, company management, creditors, government, employees and other internal and external stakeholders related to their rights and obligations. Its basic principles is to make progress of company's financial performance. The better corporate governance, the better the company's performance.

Corporate governance is a key element to increase economic efficiency. It includes a series of relationships between company management, the board of directors, shareholders and other stakeholders. This underlines the value of monitoring management performance and management accountability. The management could be more focused in achieving their goals and not be engrossed with things beyond the targets.

Bulandari (2015), and Setyawan and Putri (2013) argued that good corporate governance has a positive influence on performance. This means that the better the application of good corporate governance, the better the performance of the Village Credit Institutions. This underlies another hypothesis of this study that:

H2: Corporate governance has a positive effect on the performance of Village Credit Institutions

RESEARCH METHOD

This study used a Likert scale outlined in the questionnaire to measure the dependent and independent variables. The dependent variable of LPD's performance is measured by questions regarding financial performance and management performance. The independent variable is the intellectual capital of the institutions. Intellectual capital is measured based on three components including human capital, structural capital and relational capital. Corporate governance is measured by focusing on five principles of corporate governance, including transparency, accountability, responsibility, independence and fairness. This study was conducted in Tampaksiring, Gianyar, Bali. The study population was 32 LPDs with 96 respondents, consisting of the institution heads, cashiers, and accounting staffs.

The data analysis began with testing the validity and reliability of research instruments to obtain relevant results. The data were then analyzed by multiple linear regression analysis to obtain a comprehensive picture of the effect of intellectual capital, and good corporate governance on LPD's performance.

RESULTS AND DISCUSSION

The data analysis with a multiple linear regression technique showed the results as in Table 1.

Table 1. The Results of Multiple Linear Regression Analysis

Variable	Regression coefficient	t-value	sig
Constants	-0.916		
Intelectual capital	0.132	2.207	0.030*
Corporate governance	0.369	4.627	0.000*
R^2	0.844		
Adj R^2	0.713		
F-value	56.414		
Sig	0.000*		

Note. **p* < .01, ***p* < .01

The analysis results above signify that intellectual capital has a positive and significant effect on LPD's performance. The t test results show a significance value of 0.030, which is smaller than α 0.05, implying the first hypothesis is accepted. It means the better the intellectual capital of a company or institution, the better the performance. Intellectual capital is an intangible fixed asset leveraging stakeholders' trust in the company or institution. It is a set of intangible resources to drive organizations to improve their performance and value. Those LPDs have adequate intellectual capital such as employee knowledge, good relations with indigenous villagers, and good organizational management.

Additionally, the results of t test indicate that corporate governance has a significance value of 0,000, which is smaller than α 0.05. It signifies that the second hypothesis is accepted. It conveys the better the implementation of corporate governance, the more increasing the company's performance. Corporate governance is one key element to increase economic efficiency. It includes a series of relationships between company management, the board of directors, shareholders and other stakeholders. The LPDs have lived the principles of corporate governance, comprising transparency, accountability, responsibility, independence and fairness. With their good corporate governance, they are highly able to improve their financial and management performance.

CONCLUSIONS

The analysis and discussion above lead to conclusions that intellectual capital and corporate governance have a positive effect on LPDs performance. Tampaksiring LPDs have broad-minded employees, comfortable and adequate infrastructures, and effective communication built among customers and other parties. These all do increase their outstanding performance. Good corporate governance principles applied in the LPDs' management is one of the key elements in increasing the effectiveness of organizational management and economic efficiency.

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