The Effect of Corporate Governance, Financial Ratio, and Macroeconomics on Financial Distress (Study of Property and Real Estate Sector Companies Listed at The IDX In 2017–2021)

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Abstract. This research aims to investigate the impact of corporate governance, financial ratios, and macroeconomic factors on financial distress within the property and real estate sector companies listed on the Indonesia Stock Exchange (IDX) from 2017 to 2021. The study employs a regression analysis methodology utilizing a sample of property and real estate companies during the specified period. Data was collected from the companies' financial reports and relevant macroeconomic indicators. The study results show that H2, H3, H4 and H5 influence financial distress. However, for H1 and H6, it does not affect the occurrence of financial distress.

Keywords: Corporate Governance, Financial Ratio, Macroeconomics, Financial Distress

1 Introduction

The property and real estate sector is one of the sectors that is the focus of the Indonesian economy. The property and real estate sector often faces heavy debt burdens due to dependence on external financing. Dependence on external financing can make the property and real estate sector more vulnerable to financial risks and market fluctuations. Before the company enters the bankruptcy phase, it first experiences financial distress, namely a situation that arises when the company's finances are in a bad condition and crisis so that the company has difficulty fulfilling its obligations [10]. Support from a study conducted by [20] states that financial difficulties can occur due to a series of errors, inappropriate decisions, and interrelated weaknesses that can result in direct or indirect damage to management, as well as a lack of effort to resolve financial problems so that the use of funds do not match the needs of the company. Therefore, researchers must include non-financial factors such as macroeconomic conditions and corporate governance as the focus of research to improve research accuracy.

Corporate governance is a system that regulates, controls and monitors business control processes to increase share value and be of concern to stakeholders, employees and the surrounding community [1]. The use of effective corporate governance mechanisms can prevent companies from experiencing financial difficulties, improve internal control, and make good use of shareholder interests which has an impact on protecting corporate. So, in this study, corporate governance will be proxied by managerial ownership also institutional ownership.

ICEBE 2023, September 13-14, Bandar Lampung, Indonesia

DOI 10.4108/eai.13-9-2023.2341135

In a complex and competitive company situation, other variables that can provide a more credible analysis can also be used in financial ratios. Financial ratios can see the company's financial position in the future, it’s can be helping full for making the right decision. Hossein [27] states that by using financial ratios, stakeholders will gain better insight into the company's financial condition, pay attention to possible problems that will arise in the future, identify trends and performance patterns, and compare company performance with competitors in the same industry with the help of financial statements. So, in this study, the financial ratio will be proxied by leverage and profitability.

Another external factor that is also important to note in analyzing financial distress is the macroeconomics that reflects the state of a country. Understanding a country's macroeconomic conditions, such as inflation, exchange rates, inflation, and political stability can influence investment decisions and a company's business strategy. For example, through macroeconomic analysis, the government can formulate fiscal and monetary policies to control inflation, reduce unemployment, and encourage economic growth. So, the macroeconomics in this study will be proxied by inflation and exchange rates.

Through this research, researchers will conduct an in-depth analysis of corporate governance, which is proxied by managerial ownership and institutional ownership; financial ratios will be proxied by leverage and profitability, and macroeconomics will be proxied by inflation and exchange rates facing financial distress, which combines internal variables. and external to provide more credible results because this approach helps in identifying sources of risk from within and outside the company so that the company can deal with it more effectively. This research will also analyze the company to be more proactive in identifying potential financial problems and taking preventive or remedial steps before the situation worsens. This helps companies to prevent the risk of financial distress and minimize its negative impact.

2 Literature review

Managerial Ownership

Managerial ownership means that the leader or director of the organization holds shares in the organization. In managerial ownership, the managers or directors buy company shares to own part of the company and gain profits from the company's operational activities. [19] reveals that managerial ownership can increase management's motivation to take actions that benefit the company and shareholders because managers are directly interested in the company's success.

However, in certain cases, high managerial ownership can also contribute to the risk of financial distress. High managerial ownership can give rise to conflicts of interest between managers and external shareholders. Managers with significant shareholdings may take higher risks to increase the value of their shares.

Studies conducted by [50] and [14] show that managerial ownership does not affect the condition of financial difficulties in companies. Managerial ownership in companies is sometimes only used to attract investors, to increase investor interest in investing. This is due to investors' view that management will maximize the profits obtained. However, other findings that are different from this research ([42]; [15]; [48]) state that managerial ownership affects the condition of financial difficulties in companies. This illustrates that if managerial ownership is large in a company, the occurrence of financial difficulties will be lower. So that it can be determined the formulation of the hypothesis as follows:

H1: Managerial ownership has a positive effect on financial distress.

Institutional Ownership

Agency theory explains that agents may act outside the interests of shareholders and the company due to the desire to enrich themselves. Thus, several controls are needed that can pressure agents to act in this way, one of which is the existence of share ownership for parties outside the company's management [44]. Institutional ownership means that entities outside the company, such as financial institutions, for-profit companies, and investment companies, shareholders in these companies.

Institutional ownership can be an important indicator of a company's financial health and potential bankruptcy risk. The greater the institutional investment in the company, the larger the company will achieve good financial performance and the smaller the risk of bankruptcy due to balanced external supervision and better execution. Research conducted by [50] reveals that having high institutional ownership can increase control activities within the company, enabling company management to remain more proactive and professional.

H2: Institutional ownership harms financial distress

Leverage

Leverage is a calculation that measures a company's ability to pay long-term and short-term obligations when the company is liquidated or dissolved. The higher the leverage in a company, the higher the risk of financial distress. This is due to fixed costs for paying debt interest, which the company must pay even if sales or profits fall [22]. If the company has difficulty paying its debts then the company experiences serious financial problems. Therefore, companies should pay attention to good leverage risk management to prevent the risk of financial difficulties.

If a company has high leverage, according to [31], this can put the company in danger because the more debt it has, of course, will make it difficult for the company to pay off its obligations. By having a high leverage value, it can be stated that the company has not been able to fund its business using only the company's funds. As the assumption of the pecking order theory, in this case, the company will choose to do internal financing if it can. This is because choosing external funding, which is usually in the form of debt, will increase the leverage a company has

H3: Leverage has a positive effect on financial distress.

Profitability

Profitability provides information about the company in obtaining operational profits from every sale generated, or it can be said to be a net final result of various existing decisions and policies. In [54], the higher the profits a company gets, the less likely the risk of financial distress occurs. This is because the greater the profits, the better the company can meet its financial obligations, such as debt repayment and operational costs.

According to [31], profitability harms financial distress. This means that when the level of profitability achieved by the company is higher, the better the company's financial performance will be, so that the company will be further away from financial distress. In addition, companies with large profits usually have positive cash flow and sufficient cash reserves to deal with crises.

Several studies, such as those conducted by [33], [19], [47] and [29] show that profitability ratios harm financial distress. This is because if a company's profitability level is

getting bigger, its will pe impact the probability of the company to facing the financial distress, and vice versa.
H4: Profitability harms financial distress

Inflation

Inflation is a situation that increasing prices of goods on an ongoing basis. High inflation can harm companies experiencing financial difficulties (Hadi, 2014). One of the main effects of inflation is general depreciation. When a company experiences difficulties meeting its financial obligations during a period of financial distress, exchange rate depreciation can weaken its financial position.

When a company cannot adjust the price of its product or service to meet rising production costs, its profits can fall. If the company is already facing financial distress, its will be decrease in profits and get worsen the company's financial situation. Studies conducted by [38] and [49] reveal that inflation, which causes an increase in the price of goods, can reduce people's purchasing power. This situation impacts declining demand for shares, so stock prices and returns also fall. If this condition continues for a long time, the income of the company will decrease and the risk of the company experiencing financial distress will increase. Studies conducted by [44] and [36] show that price increases generally harm financial distress.
H5: Inflation has a positive effect on financial distress

Exchange rate

The exchange rate is a situation that can provide information about the stability of a country's economy. An increase in the value of a country's currency or an appreciation of the value of foreign currency will also increase a country's economy. [49], the exchange rate impacts financial distress. A strong exchange rate can reduce the risk of financial difficulties in a country or company experiencing financial difficulties.

In the long term, a company's sales profits will increase, this is accompanied by a reduced risk of financial distress. Also when a country's exchange rate weakens, the purchasing power of that currency weakens. Research by [52] states that in the economy, companies have higher production costs for imported raw materials, and product export revenues decrease. This can reduce a company's sales and profits and increase the risk of financial distress.

The results of research conducted by [49] show that the exchange rate significantly influences financial difficulties. The weakening Rupiah exchange rate will have an impact on the activities of companies that use foreign currencies in their financial reports. Companies will spend more Rupiah if they carry out transactions in foreign currency. Therefore, the higher the rupiah exchange rate is against foreign currencies, the greater the potential for a company to experience financial distress.
H6: The exchange rate harms financial distress

3 Methodology and Data Analysis

Samples and Data

The research sample is a property and real estate sector company listed on the Indonesia Stock Exchange (IDX) in 2017 - 2021. The sampling of this study method used was purposive sampling. This data collection technique is based on certain considerations [51]. The sample used in the study consisted of 25 companies.

Hypothesis test

This study tested the hypothesis using descriptive statistical analysis, multiple linear regression analysis, and the classical assumption test. This test uses the SPSS 25 statistical tool. The formula for multiple linear regression in this study is as follows:

$$FD_{i,t} = \alpha + \beta_1 KM_{i,t} + \beta_2 KI_{i,t} + \beta_3 DER_{i,t} + \beta_4 ROA_{i,t} + \beta_5 INF_{i,t} + \beta_6 NT_{i,t} + e$$

Information:
FD = Financial distress
α = Constant
β1 - β8 = Regression coefficient of each proxy
MO = Managerial Ownership
MI = Institutional Ownership
DER = Debt to Equity Ratio (DER)
ROA = Return on Assets (ROA)
INF = Inflation
ER = Exchange Rate
E = term error

4. Research Results And Discussion

Descriptive Statistics.

Table 1. Descriptive Statistics

	N	Min.	Max.	Mean	Std. Deviation
MO	125	.00000	.62953	.0650326	.16500237
MI	125	.37047	1.00000	.9349674	.16500237
DER	125	.02121	2.51879	.7188473	.52843447
ROA	125	-.18581	.37516	.0296651	.06321567

INF	125	.01680	.03610	.0260200	.00737077
ER	125	9.18390	9.28464	9.2416966	.03426334
FD	125	-3.09890	134.37312	6.9508117	13.99096740
Valid N (listwise)	125				

Source: Processed data, 2023 (SPSS output)

The results of the descriptive analysis indicate that the number of samples used in the study, there were 125 samples. The managerial ownership variable has a min value of 0.00000, a max value of 0.62953, a mean of 0.0650326 and a standard deviation of 0.16500237. The institutional ownership corporate variable has a min value of 0.37047 and a max value of 1; the mean indicates 0.9349674 with a standard deviation of 0.16500237.

The leverage variable has a min value of 0.02121, a max value of 2.51879, a mean of 0.7188473, and a standard deviation of 0.52843447. The profitability variable has a min value of -0.18581 and a max value of 0.37516; the mean indicates 0.0296651 with a standard deviation of 0.06321567.

The inflation variable has a min value of 0.01680, a max value of 0.03610, a mean of 0.0260200 and a standard deviation of 0.00737077. The exchange rate variable has a min value of 9.18390, a max value of 9.28464, a mean of 9.2416966, and a standard deviation of 0.03426334.

Classic Assumption Test

a. Normality Test

The results of the normality test give an Asymptotic significance (2-tailed) value in the 2017-2021 data of 0.200 > 0.05. This means that the data in this study are normally distributed

Table 2. Normality Test Results

One-Sample Kolmogorov-Smirnov Test	
Asymp. Sig (2-tailed)	0,200[c,d]

Source: Processed data, 2023 (SPSS output)

b. Mutikolinearity Test

Table 3. Multikolinearity Test Results

Model		Collinearity Statistics	
		Tolerance	VIF
1	(Constant)		
	MO	.949	1.053
	MI	.936	1.068
	DER	.874	1.144
	ROA	.820	1.219
	INF	.872	1.146
	ER	.922	1.085

Source: Processed data, 2023 (SPSS output)

After inspection, it was found that the obtained multicollinearity VIF values ranged from 1.053 to .d. 1.219, while the tolerance is between 0.820 and d. 0.949. The conclusion of this test is that there is no multicollinearity in the study data and the independent variables can be used as predictor variables. If you note Table 3 above, the VIF number (variance inflation factor) < 10 and the tolerance number > 0.10, it can be interpreted that there is no perfect linear relationship between the independent variables. The data used in this study do not suffer from multicollinearity symptoms, and the regression model formed is suitable for predicting financial distress.

c. Heteroscedasticity Test

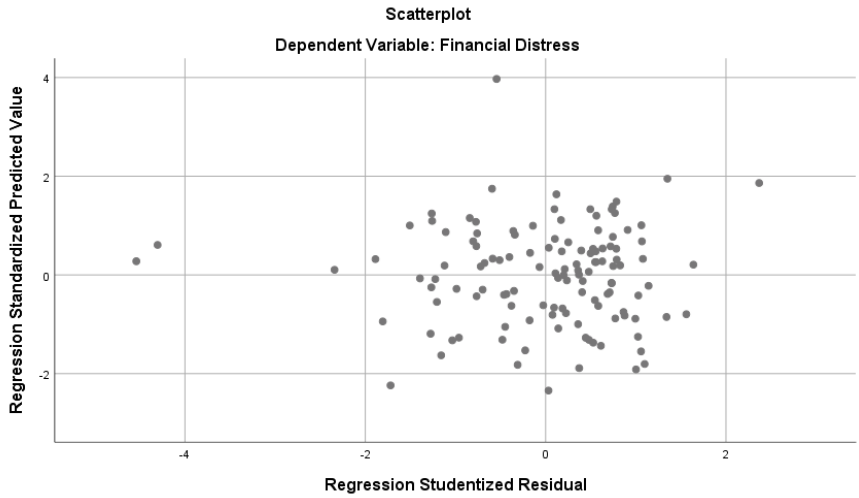

Figure 1. Heteroskedasticity Test Results
Source: Processed data, 2023 (SPSS output)

As can be seen from the figure above, the points around the number 0 on the Y-axis are distributed below and above the number 0 on the Y-axis, and do not form a specific pattern. So there is no heteroscedasticity in this regression model.

d. Autocorrelation Test

Table 4. Autocorrelation Test Results

Durbin-Watson
2.192

Source: Processed data, 2023 (SPSS output)

Looking at Table 4, the autocorrelation test results above show that:

d = 2,192

n = 125

k = 6

dL = 1,6089

dU = 1,8096

4-dL = 2,3911

Then dU < d < 4-dL = 1.8096 < 2.192 < 2.3911

According to Table 4 above, the Durbin-Watson value 2.192 is larger than the upper limit (dU) (i.e. 1.8096), and smaller than the 4-dU value (i.e. 2.3911), 125 samples from 6 variables (n = 125, k = 6), The significance level is 0.05. From the results of the Durbin-Watson autocorrelation test, it can be concluded that there are no problems or symptoms of autocorrelation and the requirement of dU < d < 4-dL is met.

Hypothesis Testing

T-test

This test was carried out using a significance level of α = 0.05. The following results of testing the partial regression model (t-test) can be seen in the following table:

Table 5. T-Test Results

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	53.858	138.677		.388	.698
	MO	.046	.087	.034	.521	.604
	MI	9.633	3.084	.206	3.124	.002
	DER	-9.804	.997	-.670	-9.838	.000
	ROA	-21.849	8.597	-.179	-2.541	.012
	INF	187.409	71.502	.179	2.621	.010
	ER	-5.745	14.965	-.025	-.384	.702

Source: Processed data, 2023 (SPSS output)

From the test results, the regression equation obtained is as follows:

FD = 53.858 + 0.46 KI + 9.633 KM – 9.804 DER - 21.849 ROA + 187.409 INF – 5.745 NT + e

For the results of the H1 test, the probability value obtained is 0.604 or greater than the significance level α=0.05 (5%); this indicates that the first hypothesis is not supported. H2 obtains a probability result of 0.002 or less than 0.05. It can be concluded that the second hypothesis is supported. The probability result of the H3 test is 0.000 or less than 0.05. It can be concluded that the third hypothesis is supported. The probability result of the H4 test is 0.012 or less than 0.05. It can be concluded that the fourth hypothesis is supported. The probability result of the H5 test is 0.10 or less than 0.05. It can be concluded that the fifth hypothesis is supported. The probability result in the H6 test is 0.702 or greater than 0.05. It can be concluded that the sixth assumption does not hold.

5. Implications and Suggestions for Further Research

The H1 test shows that company ownership has no impact on a company's financial difficulties. Company management's equity stakes are sometimes used solely to attract investors with the goal of increasing investor interest. This is because investors believe that a company's management will work hard to maximize the company's profits. The H2 test shows that institutional ownership affects a firm's financial distress. Institutional ownership has a significant negative impact, which may also be caused by tighter regulation of financial institutions such as pension funds, mutual funds, and insurance companies. Other shareholder parties often also have resources and expertise that enable them to exercise greater oversight of the company in which they own shares. The relationship between institutional ownership and financial distress can be explained because if institutional investors own the company, then the company's management cannot hide the losses or failures experienced, which triggers financial distress.

The H3 test shows that leverage has a positive effect on financial distress. These results reflect that greater interest payments usually accompany high debt. If a company faces poor financial performance or declining revenues, paying interest on debt can become even more difficult. High-interest expenses can affect a company's ability to meet its financial obligations, increasing the risk of financial distress. The H4 test shows that profitability harms financial distress. High profitability indicates that the company can generate significant profits from its assets. This usually reflects good operational efficiency and the ability to generate sufficient revenue to cover operating expenses and servicing debt. High profitability also often reflects the company's financial stability.

The H5 test means that the inflation variable affects financial distress. The increase in inflation can cause the company's operational costs to increase. Prices of raw materials, labour and other components may rise, reducing a company's profit margins. If a company cannot price a product or service balanced, higher costs can hurt profitability, increasing the risk of financial distress. The H6 test shows that the exchange rate does not affect financial distress. Most of the business transactions and income of companies in Indonesia's property and real estate sector come from the domestic market; fluctuations in exchange rates may be felt less than companies that rely more on international transactions. This can help reduce exchange rate risk exposure. Property and real estate transactions in Indonesia are usually carried out in the local currency, Rupiah. This means that companies in this sector may have less exposure to exchange rate risk than companies more involved in international trade.

Future research will be better if the sample's scope is based not only on the property and real estate sector listed on the IDX but on all IDX companies and other public companies. In

addition, research variables are more diverse, and research is also advised to extend the period of the research sample to obtain more significant results.

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