Does internal corporate governance mechanism control firm risk? Evidence from Indonesia's three high-risk sectors

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Corporate Governance
ISSN (International Standard Serial Number): 1472-0701
Publication date: 2 December 2019

Abstract

Purpose

This study aims to examine the control of corporate governance towards firm risks for a sample of Indonesian firms in agriculture, mining and property industries. This study highlights the impact of four indicators of internal mechanism of corporate governance, i.e. board size, board independence, board gender and board ownership, on three measurements of firm risks, i.e. total risk, asset return risk and idiosyncratic risk.

Design/methodology/approach

Panel data analysis is conducted using a sample of 62 companies of agriculture, mining and property industries listed in Indonesia Stock Exchange from 2013 to 2017. Pooled ordinary least square with hetero-corrected is the statistical approach conducted to test the hypotheses.

Findings

The result indicates that board size and board gender insignificantly influence firm risks. While board independence gives varied impacts towards firm risks, it gives positive influence towards total asset return risk, insignificant towards idiosyncratic risk and negative towards total risk. Other interesting results are found in board ownership that has insignificant influence on asset return risk and negative influence on idiosyncratic and total risk.

Research limitations/implications

Firms should incorporate corporate governance, especially the impactful roles of board independence and board ownership as they serve as tools in reducing firm risk. Moreover, investors may have a better understanding of corporate governance and factors that are influencing firm risks. Therefore, this study can assist them

various types of risks facing the company. Total risk measures both the internal and external risks, while asset return risk gives another perspective using overall market perception about the equity and assets of the company. Finally, this study also measures internal risk, which is the only risk that can be controlled and minimised by the board of the company.

Keywords

Corporate governance
Firm risks
Idiosyncratic risk
Asset return risk
Total risk

Citation

Hatane, S., Supangat, S., Tarigan, J. and Jie, F. (2019), "Does internal corporate governance mechanism control firm risk? Evidence from Indonesia's three high-risk sectors", *Corporate Governance*, Vol. 19 No. 6, pp. 1362-1376. https://doi.org/10.1108/CG-02-2019-0071

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Publisher: Emerald Publishing Limited