TPM Vol. 32, No. S4, 2025
ISSN: 1972-6325
https://www.tpmap.org/

Open Access

GOOD CORPORATE GOVERNANCE AS A MODERATOR IN THE RELATIONSHIP BETWEEN FINANCIAL RATIOS AND PROFITABILITY OF ISLAMIC COMMERCIAL BANKS IN INDONESIA

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Abstract
This study aims to analyze the role of Good Corporate Governance (GCG) as a moderating variable in the relationship between financial ratios and profitability of Islamic commercial banks in Indonesia. The financial ratios used include the Financing to Deposit Ratio (FDR) and Operating Expenses to Operating Income (BOPO), while profitability is measured using Return on Assets (ROA). This research employs a quantitative approach using secondary data in the form of annual financial reports from 13 Islamic commercial banks during the period 2019–2024. Data analysis was conducted using the Partial Least Squares (SmartPLS 3) technique. The results indicate that FDR has a positive but insignificant effect on ROA. In contrast, BOPO has a negative and significant effect on ROA, indicating that operational efficiency is a key factor in enhancing the profitability of Islamic banks. Furthermore, GCG does not exhibit a significant moderating effect on the relationship between FDR and BOPO with ROA. These findings suggest that strategies to improve profitability should focus on controlling operational costs and strengthening the quality of financing, while still adhering to the principles of good governance.

Keywords: Return on Assets, Financing to Deposit Ratio, Operating Expenses to Operating Income (BOPO), Good Corporate Governance, Islamic Commercial Banks.

INTRODUCTION

The development of Islamic banking in Indonesia has shown a positive trend, as reported by the otoritas jasa keuangan (2024). However, challenges in enhancing profitability remain a primary concern. Profitability, which is commonly measured by Return on Assets (ROA), reflects a bank's efficiency in managing its assets to generate profits (Kasmir 2017). In the context of Islamic commercial banks, several financial factors such as the Financing to Deposit Ratio (FDR) and Operating Expenses to Operating Income (BOPO) play a significant role in influencing profitability performance.

FDR illustrates the proportion of third-party funds that are distributed in the form of financing. A higher FDR indicates a greater financing risk, but it also has the potential to increase income if managed properly (Antonio 2001). On the other hand, the BOPO ratio reflects the bank's operational efficiency; it shows the amount of cost incurred to generate income. A high BOPO ratio may indicate low efficiency, which can negatively affect profitability (Ismail 2010).

In relation to the influence of financial ratios on profitability, Good Corporate Governance (GCG) can serve as a moderating factor that either strengthens or weakens this relationship. When implemented effectively, GCG is believed to enhance oversight, transparency, and accountability, thereby mitigating risks and improving the bank's financial performance (2015). Therefore, it is important to examine the role of GCG in moderating the relationship between FDR and BOPO on ROA in Islamic commercial banks in Indonesia.

LITERATURE REVIEW

Grand Theory

This study is grounded in Agency Theory and Stakeholder Theory as the grand theories. Agency Theory,

proposed by Jensen & Meckling (1976), explains that the relationship between owners (principals) and managers (agents) in an organization has the potential to create conflicts of interest due to differing objectives. Therefore, monitoring mechanisms such as Good Corporate Governance (GCG) are necessary to minimize agency costs and enhance efficiency and profitability in banks. Meanwhile, Stakeholder Theory, developed by Freeman (1984), emphasizes that companies—including Islamic banks—are accountable not only to shareholders but also to all stakeholders, such as customers, regulators, and the broader community. Consequently, effective implementation of GCG is not only aimed at optimizing financial performance through financial ratios such as CAR, FDR, NPF, and BOPO toward ROA, but also at maintaining public trust and ensuring business sustainability in an ethical and transparent manner.

Return on Assets (ROA)

Brigham & Houston (2015) explain that profitability ratios reflect a set of indicators that combine the effects of liquidity, asset management, and debt utilization on a company's operational performance. Furthermore, Kasmir (2017) states that Return on Assets (ROA) is used to measure a company's ability to generate profit from all of its assets. This ratio indicates the amount of net income earned for every rupiah of assets utilized.

Financing Deposit Ratio (FDR)

The Financing to Deposit Ratio (FDR) is a ratio used to measure a bank's ability to meet its liquidity obligations, particularly in repaying funds collected from customers. This ratio reflects the extent to which third-party funds are distributed in the form of financing (Kharazi 2022).

Operating Expenses to Operating Income (BOPO)

BOPO (Operating Expenses to Operating Income) is a ratio used to assess the efficiency and effectiveness of a bank's operational performance. This ratio reflects the extent to which bank management is able to control operating expenses in generating operating income. The lower the BOPO value, the more efficient the bank's performance (Setyarini 2020).

Good Corporate Governance (GCG)

Good Corporate Governance (GCG) has become one of the non-financial aspects that investors increasingly consider when assessing a company's feasibility before making investment decisions. Companies that implement GCG principles are generally perceived more positively by investors, as good governance reflects sound corporate performance and has the potential to enhance firm value (Laba et al. 2023).

Previous Research

FDR (X1) against ROA (Y)

The findings of Amalia et al. (2021) indicate that FDR has a significant positive effect on ROA in the context of commercial banking in Turkey. In contrast, Hasibuan et al. (2022), in a study of Islamic banks in Indonesia during the 2015–2021 period, found that the FDR variable has a significant negative effect on ROA.

BOPO (X2) against ROA (Y)

The study by Setyarini (2020) shows that an increase in BOPO leads to a decrease in ROA, indicating inefficiency in managing operational expenses. Furthermore, research by Saputra & Angriani (2023) states that BOPO has a significant negative effect on ROA, highlighting the importance of cost management in banking operations.

GCG (Z) moderates FDR (X1) on ROA (Y)

Dewi et al. (2016) found that Good Corporate Governance (GCG) has no significant effect on Return on Assets (ROA), and therefore does not moderate the relationship between the Financing to Deposit Ratio (FDR) and ROA. This finding is supported by Sulbahri et al. (2022), who also found that GCG does not moderate the relationship between FDR and ROA in the banking companies examined.

GCG (Z) moderates BOPO (X2) on ROA (Y)

Liu & Cortes (2015) found in their study that the better the quality of GCG, the weaker the negative impact of BOPO on ROA. Furthermore, Harahap & Hairunnisah (2017) showed that GCG was not proven to moderate the relationship between BOPO and ROA.

Conceptual framework and hypotheses

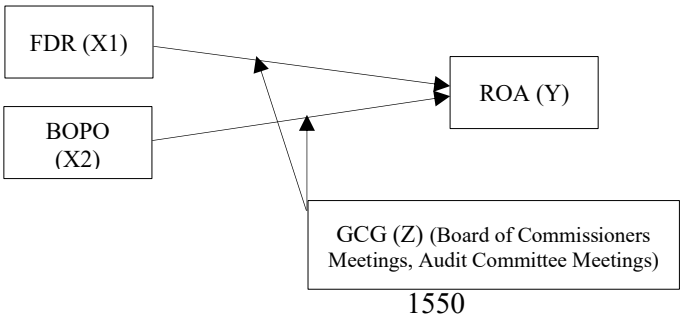

Figure 1 : Conceptual framework

pengembangan hipotesis
H1 : FDR is suspected to have a positive and significant effect on ROA
H2 : BOPO is suspected to have a negative and significant effect on ROA
H3 : GCG is presumed not to moderate the relationship between FDR and ROA
H4 : GCG is suspected to moderate the relationship between BOPO and ROA

METHODOLOGY

Population and Sample
The population in this study includes all Islamic banking offices in Indonesia, consisting of Islamic Commercial Banks and Sharia Business Units, with a total of 47 banks. The sample criteria in this study focus on the Islamic banking industry classified as Islamic Commercial Banks, comprising 13 banks in 2024. The observation period spans from 2019 to 2024.
Data types and sources
This study uses quantitative data obtained from officially published financial reports accessed through the websites of each Islamic Commercial Bank in Indonesia.
Data Analysis Methods
This study employs SmartPLS to analyze both direct and moderating effects, using the following data processing techniques:
Outer Model : Convergent Validity, Average Variance Extracted (AVE), Composite Reliability, Discriminant Validity
Inner Model : R-Square, Hypothesis Testing, Goodness of Fit Index

RESULTS AND DISCUSSION

Outer Model Test
Convergent Validity Test
Table 1. Outer Loadings of Each Variable

Construct	Item Code	Loading Factor	Description
FDR (X1)	FDR	1.000	Valid
BOPO (X2)	BOPO	1.000	Valid
GCG (Z)	RDK	0.959	Valid
	RKA	0.769	Valid
ROA (Y)	ROA	1.000	Valid

Source: Processed data based on SmartPLS 3 output, 2025
The results show that all indicators have loading factor values above 0.7, with some even reaching 1.000. This indicates that each indicator is able to represent its respective construct well, leading to the conclusion that the research instrument meets the criteria for convergent validity.
Average Variance Extracted (AVE) and Composite Reliability (CR) Test
Table 2. Average Variance Extracted and Composite Reliability Test

Variable	AVE	CR
FDR (X1)	1.000	1.000
BOPO (X2)	1.000	1.000
GCG (Z)	0.756	0.859
ROA (Y)	1.000	1.000

Source: Processed data based on SmartPLS 3 output, 2025
The AVE values for all variables are greater than 0.5, and the CR values exceed 0.7. This indicates that each construct has good internal consistency and is able to adequately explain the variance of its indicators. In other words, the model demonstrates strong reliability.
Discriminant Validity Test
Table 3. Discriminant Validity Test Using the Fornell-Larcker Criterion

Construct	BOPO (X2)	FDR (X1)	GCG (Z)	ROA (Y)

BOPO (X2)	-0.007			
FDR (X1)	1.000	1.000		
GCG (Z)	-0.261	-0.122	0.869	
ROA (Y)	-0.734	0.220	0.119	1.000

Source: Processed data based on SmartPLS 3 output, 2025

The test results show that the square root of the AVE for each construct is greater than the correlations with other constructs. This indicates that each variable is clearly distinct from the others, thereby confirming that the instrument meets the criteria for discriminant validity.

Inner Model Test

R-Square Test

Table 4. R-Square Test

Variable	R-Square
ROA (Y)	0.602

Source: Processed data based on SmartPLS 3 output, 2025

An R-Square value of 0.602 indicates that the independent variables in the model are able to explain 60.2% of the variation in ROA, while the remaining 39.8% is influenced by other factors outside the model.

Hypothesis Testing

Table 5. Hypothesis Testing

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values
FDR -> ROA	0.252	0.284	0.243	1.035	0.304
BOPO -> ROA	-1.402	-1.321	0.607	2.310	0.024
Moderating Effect 1 -> ROA	0.065	0.138	0.290	0.224	0.823
Moderating Effect 2 -> ROA	-0.725	-0.642	0.727	0.998	0.321

Source: Processed data based on SmartPLS 3 output, 2025

H1: FDR is suspected to have a positive and significant effect on ROA

The research findings indicate that the effect of FDR on ROA is positive but not significant, as evidenced by a p-value greater than 0.05. Therefore, hypothesis **H1 is not supported.**

H2: BOPO is suspected to have a negative and significant effect on ROA

The findings of this study indicate that BOPO has a significant negative effect on ROA, meaning that an increase in BOPO will decrease ROA performance. Therefore, hypothesis **H2 is supported and accepted.**

H3: GCG is presumed not to moderate the relationship between FDR and ROA

The first moderating effect shows a positive direction but is not significant. This indicates that GCG neither strengthens nor weakens the relationship between FDR and ROA. Therefore, hypothesis **H3 is accepted.**

H4: GCG is suspected to moderate the relationship between BOPO and ROA

The second moderating effect shows a negative direction and is not significant, indicating that GCG does not influence the relationship between BOPO and ROA. Therefore, hypothesis **H4 is rejected.**

Goodness of Fit Index

Table 6. Goodness of Fit Index Test

	Saturated Model	Estimated Model
SRMR	0.048	0.051

Source: Processed data based on SmartPLS 3 output, 2025

The SRMR value of 0.051 is below the threshold of 0.08, indicating that the model has a good fit.

DISCUSSION

The research results show that FDR has a positive but not significant effect on ROA, meaning that the increase in financing has not consistently boosted profitability. This aligns with the condition of Islamic banking in Indonesia, which still faces challenges related to financing quality and non-performing financing (NPF) risk. Meanwhile, BOPO has a significant negative effect on ROA, indicating that

controlling operational costs is key to maintaining profitability. Both moderating variables are not significant, highlighting the need to focus on service digitalization strategies, product innovation, and the strengthening of risk management.

Islamic bank management must improve the quality of financing through risk mitigation and the selection of productive financing sectors so that FDR can have a tangible impact on profitability. In addition, BOPO control should be carried out by enhancing operational cost efficiency, such as utilizing digital technology to reduce administrative expenses. This approach will enhance the competitiveness of Islamic banks amid intense industry competition.

CONCLUSION

Islamic banking is still in the development stage and must compete closely with conventional banks. In such conditions, cost control and risk management become key factors in improving profitability. The analysis results also indicate that operational cost efficiency is an essential aspect that needs to be addressed to strengthen financial performance. Moreover, a high level of financing must be balanced with effective risk management in order to contribute optimally to profitability.

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