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MEASURING CEO PERFORMANCE IN PT. ASTRA OTOPARTS PERIOD 2007-2014

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Abstract - Two important roles that have crucial role in the company in order to keep the company running First are the agents who runs the business, the performance of the agents are usually represented by the Chief Executive Officer. Chief Executive Officer or CEO for short is the head leader of a company. It is also common for some companies to call CEO as President of Director. CEO or President of Director's job description cannot be stated as a general because each company has their own policy. Second are the shareholders or the financiers who have the capital in order for the company to keep on going. The fund that is given is represented in stocks. The relationship between agents and shareholders is concluded in the Agency Theory. Agency theory addresses the relationship where in a contract 'one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making to the agent'. Problems will arise if there is a difference of interest between the agent and shareholders.

Keywords: Agency cost, stock prices, Chief Executive Officer, Shareholders

Introduction

The relationship between agents and shareholders is concluded in the Agency Theory. Agency theory addresses the relationship where in a contract 'one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making to the agent' (Jensen and Meckling, 1976: 308). Agents have to work on principal's behalf. The main concern of agency theory as proposed by Jensen and Meckling (1976) is how to write con- tracts in which an agent's performance can be measured and incentivized so that they act with the principal's interests in mind (cunliffle.indd, 2012). There will be a separation between ownership and control, when the owner have decided to employ managers or agents to run the business for them, the agents need to be monitored in order to keep their performance so that they will act in the owner's interest. Economists Alchian and Demsetz (1972) were the first to argue that monitoring the performance of individual work effort is always a cost of any firm and that organizational inefficiencies are created when the flow of information on individual performance is decreased or blocked. This can happen if there are large teams, unsupervised professionals, or executives of corporations who act autonomously. PT Astra Otoparts Tbk (Astra Otoparts) is the largest and foremost automotive component group of company in Indonesia, producing and distributing a wide variety of two-wheeler and four-wheeler spare parts.

Problem Statement

Problems will arise if there is a difference of interest between the agent and shareholders. Supposedly based on the agency theory, profit that has been generated from a company has to be returned fully to the owner of the company. This research focuses on how CEO of ASTRA OTOPARTS affects the financial performance of the company through regression approaches. This study aims to search for the best CEO based on the balance sheet and income statement and rank them based on their equation

This research focuses on how CEO of ASTRA OTOPARTS affects the financial performance of the company through regression approaches. The limitation of the data that is taken for this research is through the company's financial report balance sheet and income statement from 2007 – 2014. This study aims to search for the best CEO based on the balance sheet and income statement and rank them based on their equation.

Literature Review

Agency Theory

Agency relationship is one in which one or more people in this case are stated as the principals, the person who engage another people who are stated as agents to perform services on the principals behalf which involves delegating some decision on making authority to the agent. (Meckling & Jensen, 1976).

Agency theory study is the study of the agency relationship combine with the issues that arise from this type of relationship. Mainly about the dilemma that the principal and the agent would face. In a modern economy, management, and management of the company more and more separated from the ownership of the company. This is in line with the Agency Theory, which emphasizes the importance of company owners (shareholders) handed over the management of the company to the professional staff (called agents) are better understood in running the day-to-day business. The larger the company managed to obtain the greater the profit gains agents. While the owner of the company (shareholders) only oversees and monitors the running of the company are managed by the management as well as develop a system of incentives for managers of management to ensure that they work in the interest of the company (Adrian Sutedi, 2011: 13). Jensen and Meckling (1976) describes the agency relationship in the theory of agency (agency theory) that the company is a collection of contract (nexus of contract) between the owners of the resource costs (principal) and the manager (agent) who takes care of the use and control of these resources.

Agency Cost

While the agent/principal had been founded Adam Smith had pondered dilemma in a corporate context as early as the 18th century,

> "The directors of [joint-stock] companies, however, being the managers rather of other people's money than of their own, it cannot well be expected, that they should watch over it with the same anxious vigilance with which the partners in a private copartner frequently watch over their own. Like the stewards of a rich man, they are apt to consider attention to small matters as not for their master's honor, and very easily give themselves a dispensation from having it. Negligence and profusion, therefore, must always prevail, more or less, in the management of the affairs of such a company." – The Wealth of Nations, 1776."

Many of its key concepts were developed in literature on the firm, organizations, and on incentives and information—a separate theory of agency did not emerge until the early 1970s when Stephen A. Ross and Barry M. Mitnick, working independently, each presented a theory of agency. Mitnick, Barry M., Origin of the Theory of Agency: An Account By One of the Theory's Originators (January 2006). The agents also have their own problem, for example, when the agent is faced with decisions in which they have to make the decision but they have to represent their principals. Problem will come up once the agents have their own interest, which may not be the same as the principals' interest. Some compromise between the two does not coincide. Internal cost that arises from or must be paid to an agent that acted on behalf of the principal. Agency cost arises because of core problems such as conflicts of interest between shareholders and management. Shareholders wish for management to run the company in a way that will increases the shareholder's value.

“We define an agency relationship as a contract under which one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent. If both parties to the relationship are utility maximizes, there is good reason to believe that the agent will not always act in the best interests of the principal. The principal can limit divergences from his interest by establishing appropriate incentives for the agent and by incurring monitoring costs designed to limit the aberrant activities of the agent.” (Meckling & Jensen, 1976).

Income Statement

Income Statement concludes the revenues earned and subtracts the expense incurred in earning that revenue to calculate the resulting net profit or loss for a given accounting period. Income statement sometimes referred to the bottom line of a business in that it calculates the net profit or losses for a given period and reports at the last line on the Income Statement. Income Statements started with the total amount of money that is received from the sale of products or the provision services (Helfert, 2001).

Assets

Assets are bought to increase the value of a firm or benefit the firm's operations. You can think of an asset as something that can generate cash flow, regardless of whether it's a company's manufacturing equipment.

Revenue

The amount of money that a company actually receives during a specific period, including discounts and deductions for returned merchandise. It is the "top line" or "gross income" figure from which costs are subtracted to determine net income. Revenue is calculated by multiplying the price at which goods or services are sold by the number of units or amount sold. (Gitman & Zutter, 2012)

Stock

The definition of stock is as Shares in a sign of equity investment in a limited liability company (Panji & Piji, 2008). Owning the shares of a company, the investor may obtain advantages such as getting dividends, capital gains and other non-financial advantages, such as pride and power to obtain voting rights in determining the running of the company.

Fundamental Factors

Fundamental factors are factors that come from the company that issued the stock. This factor is often referred to as the company's performance, both financial performance and non-financial performance.

Earning per Shares

The portion of a company's profit allocated to each outstanding share of common stock. Earnings per share serves as an indicator of a company's profitability. Calculating EPS, the company often uses a weighted average of shares outstanding over the reporting term. The one-year (historical or trailing) EPS growth rate is calculated as the percentage change in earnings per share.

Dividend per Shares

The total amount a publicly traded company pays in ordinary dividends over a given period of time divided by the average number of shares outstanding. Dividends per share give a potential investor an idea on how much the investor will receive the dividends if the investor buys a given stock. Blue Chip Company or any other well-established companies pay high dividends per share, while on the other hand start-ups pay small dividends per share. (Harvey, 2012)

Return on Equity

The return on equity ratio or ROE is a profitability ratio that measures the ability of a firm to generate profits from its shareholders investments in the company. In other words, the return on equity ratio shows how much profit each dollar of common stockholders' equity generates.

Price to Earnings Ratio

The price/earnings multiple approaches to value is a popular technique whereby the firm's expected earnings per share (EPS) are multiplied by the average price/earnings (P/E) ratio for the industry can be obtained from a source such as Standard & Poor's industrial Ratios. The use of P/E multiples is especially helpful in valuing firms that are not publicly traded firm. In any case the price/earnings multiple approach is considered superior to the use of book or liquidation values, since it considers expected earnings (Megginson, 1997).

Weighted Avarage Cost of Capital

Weighted average cost of capital or WACC is the rate that the company is expected to pay on average to all of the company's share holders to finance the company's assets. The WACC is commonly referred to as the firm's cost of capital. It reflects the expected average future cost of capital over the long run, found by weighting the cost of each specific type of capital by it's proportion in the firm's capital structure (Gitman & Zutter, 2012).

Previous Study

Study that has been done by Yuk-Chow So entitled: "Agency Costs and Ownership Structure: Evidence From the Small Business Finance Survey Data Base" in 2005 shows that impact of managerial effectiveness on agency cost of ownership and debts in light of the variety of ownership structure, debt contract and investment. The data that was used came from 1993. It revealed that the managerial effectiveness has an important role to alleviate both agency cost of ownership and debts. This study showed that, more attention to the important role played by management to lighten agency cost of ownership in light of differences of ownership structure is needed, as well as to mitigate the debt contracts and investment policy impact on agency cost for ownership. (So, 2005)

A number of studies about agency cost is have been widely researched in many countries. Ibrahim & Samad (2011) found in Malaysia case the on average firm value are lower in family firms than non family firms, while board size, independent director and duality have a significant impact on firm performance in family firms as compared to non family firms. Besides, the governance mechanism has significant impact on agency cost for both family and non-family firms.

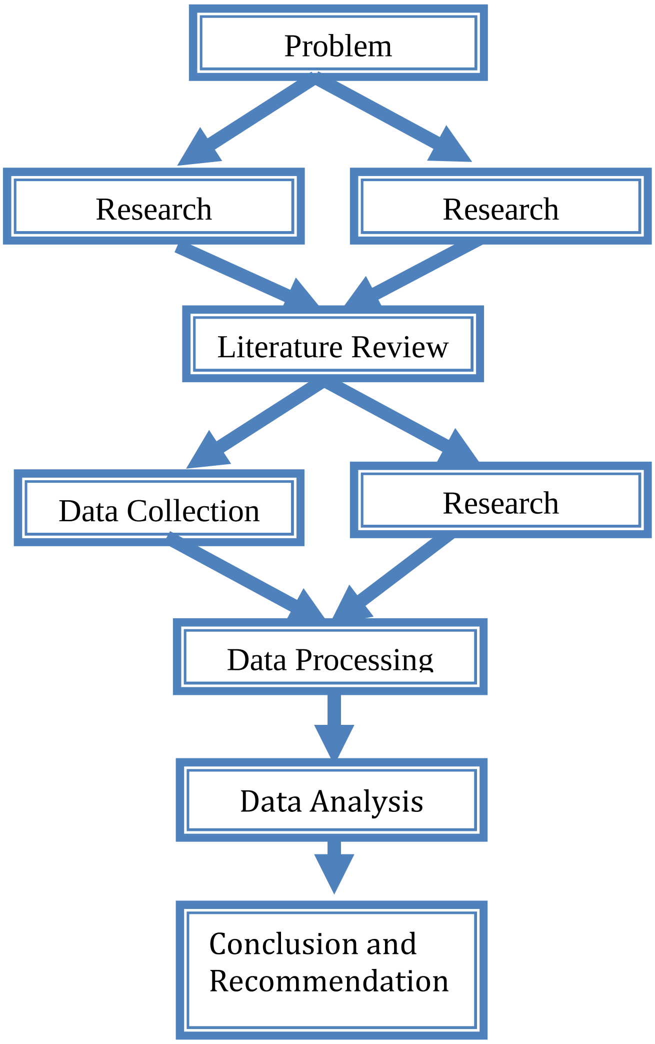
A study in Indonesia that entitled: "Agency Costs, Corporate Governance and Ownership Concentration: The Case of Agro-industrial Companies in Indonesia" was studied by Hastori, Hermanto Siregar, Roy Sembe & Tb. N Ahmad Maulana (2015). The aim of the study is to investigate the determinants of agency costs on agro-industrial firms that are listed in the Indonesian Stock Exchange (IDX). Modeling of agency costs is made and analyzed by performing regression analysis of panel data.

The result of this study show that agency costs are affected by the effectiveness of good governance mechanism, especially the function of Board of Directors (BOD) and Board of Commissioners (BOC) in conducting their responsibilities and duties, dividend payout and leverage. Although the result also shows that although Board of Directors and Board of Commissioners might have an effect towards the company's financial performance, it still considered not significant. Result of the study would help management, investors and other decision makers to implement better governance practices in agro-industrial firms in Indonesia. Based on all of the previous study, the researcher find that there is a relationship between agency costs towards the company performance that is delivered to the public as the stock price, although based on the previous studies showed that it is not significant.

Methodology

Research Design

Methodology of this research consists of several stages as follows



Problem Identification

Agency cost is one of indicator of the management system in the company. Researcher analyze the agency cost of the President Director of Astra Otoparts Tbk., determining the best President Director of a company in Indonesia has not ben developed yet in Indonesia.

Research Questions and Objectives

Researcher transcends the data used to conduct the research, then creates attention to the significance of research, and has the capacity of uniqueness of the research. Then researcher needs to make sure that the research questions that are constructed are robust to be researched.

Literature Review

At this step, researcher explores the theories behind the study to determine the variable and measurement to conduct the result

Defining Variables

This research has two kinds of variables, which are dependent and independent variables. The dependent variables will be used as Y, while the independent variables will be used, as X. Y will be represented as dependent variables, X will be represented as independent variables.

Data Collection
To achieve the research objective of this research, data wil be taken from the company's quarterly financial report. The range of the data that will be taken is from 2007 to 2014.

Data Analysis
The findings that collected from the company's annual report will be processed in the regression using dummy variable method. By looking at the last 3 Presidents of ASTRA Otoparts Eduardus Paulus Supit (2007-2009), Siswanto Prawiroatmodjo (2009-2013) and Hamdani Dzulkarnaen Salim (2013-2014), the researcher will relate the correlation between the independent variables and the dependent variables. After the number has been processed than the researcher will list all of the result in term to process the agency cost of each President Director.

Conclusions and Recommendations
This chapter summarizes about two research objectives. These are to measure and rate the agency cost of each President Directors and also to identify the best President Director based on the agency cost calculation.

Data Analysis
Descriptive Analysis
Descriptive Analysis is the discipline of quantitatively describing the main features of collection of information, or the quantitative description itself.

Classic Regression Assumptions Test
Normality Test
Normality test is done to know whether the data were taken from a population that was distributed normally. A good regression model is the one that is distributed normally or nearly to normal. If the data did not follow the spread of a normal distributed pattern, than the data are considered invalid. Normality test is done by doing Kolmogorov-Smirnov Liliefors correction test. Based on the Normality Test, all of the data is normally distributed

Autocorrelation Test
Autocorrelation test is used to detect whether there are any irrelevance of the classic assumption autocorrelation, which happens if there is a correlation between residual on the observations with other observations in the regression model. Autocorrelation test is done by doing the statistic test of Durbin Watson, According this Autocorrelation Test, than the result show there are no autocorrelations between each independent variables towards dependent.

Multicollinearity Test
Multicollinearity is something in which some or all independent variables correlated. To detect the presence or absence of multicollinearity is to use the Variance Inflation Factors (VIF). If the VIF value is below 10, and also the tolerance is greater than 0,1 than it can be concluded that there is no multicollinearity in the data. According to the result, there is no multicollinearity that is detected between Revenue, Asset, Dummy CEO_1 and Dummy CEO_2

Heteroscedasticity Test
Hetersoscedasticity test aims to test whether there is dissimilarity variance between the residual on the observations with other observations in the regression model. If the variance between the observations stays the same, than it is called homoscedasticity. Based on the calculation there is no homoscedasticity detected.

Multiple Correlation Analysis (R Square Test)
To identify the relationship between independent variables which are Revenue (X_1), Asset (X_2), D1 (X_3) and D2 (X_4) towards dependent variables (Y) which are DPS, EPS, ROE, PER and WACC, by

looking at the R^2 value. All of the result shows that all of the independent variables can relate more than 50% of the dependent variables.

Testing the Significance of Regression Coefficients

Overall Hypothetically Test
To identify whether the affect of the overall independent variables towards the dependent variable is significant. Therefore F Test is done. F test is done by two ways; the first is to know if the independent variables do affect the dependent variables, the second one is to identify whether it is significant by looking at the Sig., if it is lower than the alpha (α = 5%) than it is proven that the affect is significant. The independent turns out to be significantly affected the dependent variables.
Partially Hypothetically Test
Partially hypothetically Test needs to be done by doing T test. T test is done to calculate the significance of each independent variable partially towards the dependent variables.
Test's Criteria:
1. If T calculated ≥ T table, H_0 is refused; Ha is accepted which means that X and Y are correlated.
2. If (-T table) ≤ T calculated H_0 is refused; Ha is accepted which means that X and Y are correlated.
3. If (-T table) ≤ T calculated ≤ T table, H_0 is refused; Ha is accepted which means that X and Y are not correlated.

The result shows that almost in every factor, CEO is not that significantly affect all of the dependent variables.

Conclusion and Recommendation

Based on the data analysis, the researcher can classify what is the advantage of each CEO compare to the other CEOs. With all of the data, the researcher concludes that the best CEO among 3 CEOs of ASTRA Otoparts in the time period of 2007-2014 is Siswanto Prawiroatmodjo.

The researcher hopes that this research will be useful for those who are studying capital market, and also for shareholders. This research proofs that although it is not significant, but agency cost still caused some minor changes in the stock price, moreover aside from the fact that there is no fix calculation on how to determine the value of agency cost, it does not mean that it cannot be approached.

Calculating the agency cost of each CEO is something that could be specified as new research, therefore the researcher do hope that for further research that the scope will be expanded. Improvement can be done in further research by expanding the time period. This research can not define about the actions that were done by the CEO to affect the agency cost, improvement can be done in further research by defining all of the CEO actions towards agency cost.

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