THE EFFECT OF GOOD CORPORATE GOVERNANCE TO STOCK LIQUIDITY

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ABSTRACT: *The purpose of the company to prosper the shareholders is often constrained by conflicts of interests between owners and managers of the company. The prosperity of shareholders, which reflected in stock prices can be influenced also by the ability of stocks to be converted into cash in a short time without affecting the price (stock liquidity). Stocks that have a high level of liquidity are often indicated by information disclosure so that stock prices can adjust quickly to the actual state of the company. Conflicts of interest between owners and managers of the company can cause the level of stock liquidity to be low due to a lack of information disclosure about the company. To overcome this, the implementation of Corporate Governance will encourage companies to be more transparent in providing information. This study examines the influence of Good Corporate Governance on the level of stock liquidity by using sample companies listed in the Corporate Governance Perception Index (CGPI) in 2011-2015. The results obtained indicate that there is a significant influence of Good Corporate Governance on stock liquidity. This conclusion shows that the implementation of good corporate governance will encourage companies to provide information transparently that will increase the liquidity of the stock.*

Keywords: Corporate Governance, Stocks Liquidity, Corporate Governance Perception Index, Bid-Ask Spread

1. INTRODUCTION

The company in carrying out its operational activities has a purpose to prosper the owner of the company. This statement implies that in carrying out its operational activities the company is required to produce maximum profits. But the goal that only hopes for profit is not enough because if the company only pursue profit, it can be misinterpreted by "justifying" all ways to get profit. This will be dangerous for the company because it excludes various determinants of the survival of the company. This context is certainly not the goal of the company because the owner of the company certainly hopes his company can run forever. This condition can occur if there is a conflict of interest between the owner and the management of the company. The management of the company as the party that is given responsibility for carrying out operational activities by the owner, is likely to have a personal goal because there is no sense of ownership of the company. The absence of a goal that is inline between the owner and management of the company is referred to as Agency Problem [1].

Agency conflicts can occur because the management makes decisions that are not following the company's objectives. As a party running the company's operational activities, management has comprehensive information about the condition of the company. This will endanger the survival of the company if the owner does not have the same information as the management. This condition is often referred to as information asymmetry. There is a possibility that the management does not provide transparent information about the condition of the company to the owner, causing an agency conflict in the company. Mitchell and Meacham [2] state that the focus of agency theory is the assumption that management will act as opportunists, especially if their interests conflict with the owners.

To mitigate agency problems and improve efficiency, the implementation of good corporate governance will provide benefits for the company. The internal and external governance will encourage companies to be more disclosure and transparent, thus the level of information asymmetry will be low [3-4].

2. LITERATURE REVIEW

a) Corporate Governance

Corporate Governance is needed to avoid agency conflicts within the company. According to Claessens and Yurtoglu [5], corporate governance can be categorized into 2 definitions. The first definition emphasizes a series of behavioral aspects, such as performance, efficiency, growth, financial structure, and the treatment of shareholders and stakeholders And the second emphasizes the normative framework: Namely, regulations/regulations in which the company operates with regulations derived from sources such as the legal system, judicial system, financial markets, and the labor market. According to Sari and Riduwan [6], there are 5 basic principles of corporate governance; (1) accountability, the clarity of the functions, structures, systems, and responsibilities of each part of the company that is carried out effectively by company management, (2) Responsibility, compliance in the management of the company with the principles and rules of a healthy company, (3) Transparency, in the decision making process and openness in disclosing material and relevant information about the company, (4) Justice, fair and equal treatment in fulfilling the rights of stakeholders that arise based on the agreement and the prevailing laws and regulations, (5) Independencies, which is a situation where a company that is managed professionally does not have a conflict of interest and influence or pressure from management who do not comply with the applicable laws and regulations and the principles of a healthy company.

Fung [3] states that many investors see corporate governance as one of the key elements when they make investment decisions. If investors believe that poor corporate governance is a risk, then companies need to improve their corporate governance standards to attract investors. Beeks and Brown [7] found that companies with better governance also revealed more information. Companies that are weak in governance lack transparency and financial transparency. This condition is referred to as information asymmetry, which is a condition where there is an imbalance of information held by management and information obtained by shareholders and other stakeholders. In this condition, management tends to know more about the company than outside parties including shareholders. Thus, management has a chance to deviate which might benefit themselves.

From the OECD survey in 2005, the implementation of corporate governance in Indonesia is still weak, in which Indonesia has a lower level of governance comparing with other Southeast Asia countries. The concept of corporate governance was noticeable in Indonesia since the financial crisis of 1998. After the crisis, previous research by Wulandari and Rahman [8] conclude that the implementation of corporate governance in Indonesia is still weak.

According to Juniarti & Natalia [9], the Corporate Governance Perception Index (CGPI) is the ranking of good corporate governance by the Indonesian Institute for Corporate Governance (IICG) with SWA magazine. Companies that follow the CGPI survey showed a willingness to become a trusted and open. To promote the implementation of GCG, the Government of Indonesia (GoI) through the Indonesia Institute of Corporate Governance (IICG) has initiated to rank the level of GCG implementation [10]. Regularly, since 2001, IICG researched to evaluate GCG practices by companies. The ranking was namely Corporate Governance Perception Index (CGPI). There are ten aspects of GCG, which assessed, i.e. (1) the company's commitment on GCG, (2) transparency, (3) accountability, (4) responsibilities, (5) independence, (6) fairness, (7) competence, (8) mission statement, (9) leadership and (10) staff collaboration.

b) Stock Liquidity

Stock liquidity is the ability of a stock to change into cash quickly and without giving a big influence on the price. Liquidity plays an important role in the formation of stock prices. Stocks that have a low level of liquidity can mean having a high level of uncertainty, this factor is also a reflection that the information provided by the company is not enough for investors to make investment decisions [11].

Amihud [12] stated that liquidity has a negative relationship with stock's expected returns. Investors will demand a high level of return for stocks that have low levels of liquidity. This is due to liquidity risk for investors caused by the difficulties in trading stocks. Liquidity is an important factor in the formation of stock prices besides risk and return. Shares that have high liquidity are often associated with transparent information disclosure. Measurement of information asymmetry using the bid-ask spread shows that there is a relationship between information asymmetry and the level of liquidity, where the lower the spread indicates high liquidity [13-14].

According to Rhee & Wang [15], in an emerging market, the stock is more liquid than those in advanced economies. The lack of liquidity is regarded as a key factor for the high volatility in emerging markets and a significant impediment to financial market development.

Hypothesis Development

Previous research by Chung et al [16]; Ajina et al.[17]; Barth et al [18]; Tang & Wang [19]; Lei et al [20] state that companies with good corporate governance tend to have liquid shares because good governance increases financial and operational transparency, which in turn reduces the information asymmetry between management and fund owners. Research conducted in an emerging market has been done by Rhee & Wang [21] and Bekaert et al. [15] which stated that monitoring activities as a form of corporate governance will reduce information gaps in investors so that it will increase stock liquidity. Based on previous research, it can be concluded that corporate governance will reduce the level of information asymmetry in the company. This will make the company more transparent and reliable about any information thus it will increase the stock's liquidity in the capital market.

Hypothesis: Good Corporate Governance has a significant effect on the stock's liquidity.

3. RESEARCH METHOD

This research was conducted using sample data of companies registered in the Corporate Governance Perception Index (CGPI) in the Indonesia stock exchange period 2011 - 2015. The following are the samples in this study:

Table 1. Research Sample

No	Company
1	PT. Aneka Tambang
2	Bank Mandiri
3	Bank Negara Indonesia
4	Bank Tabungan Negara
5	PT. Timah
6	PT. Bukit Asam
7	PT. Jasa Marga

In this study the independent variable is Good Corporate Governance and the dependent variable is the stock liquidity. The measurement of these variables are as follows:

1. Good Corporate Governance will be measured using a scored assessment based on the Corporate Governance Perception Index (CGPI).
2. Stock liquidity will be measured using the formula of the bid-ask price.

The analysis technique in this study uses panel data regression analysis, with the regression equation as follows:

$LIQit = \alpha + \beta 1GCGit + eit$

Where:

LIQ = Stock's Liquidity

GCG = Good Corporate Governance

Table 2 is the result of the corporate governance index from 2011 to 2015, which was obtained from the Corporate Governance Perception Index (CGPI). Based on these data it is known that the average governance index shows an upward trend, but there was a significant decline in 2015. However, this can be caused by changes in the assessment of the governance index in a given year.

4. RESULTS AND DISCUSSION

Table 2. CGPI Index

Company	CGPI Index					
	2011	2012	2013	2014	2015	Average
PT. Aneka Tambang	64,61	86,56	88,71	88,92	71,38	80,04
Bank Mandiri	68,77	91,91	91,88	92,37	73,02	83,59
Bank Negara Indonesia	64,91	85,75	86,07	87,19	69,29	78,64
Bank Tabungan Negara	63,11	85,90	85,42	84,94	67,01	77,28
PT. Timah	50,60	75,68	77,81	80,10	64,84	69,81
PT. Bukit Asam	64,06	82,56	83,80	84,09	68,15	76,53
PT. Jasa Marga	61,98	83,66	84,52	85,16	68,28	76,72
Average	62,58	84,57	85,46	86,11	68,85	

As a further analysis, it is known that Bank Mandiri is a company that has the highest index, both annually and on average for the entire observation period. Thus, it can be concluded that Bank Mandiri is a company with a higher governance implementation compared to other companies. While the lowest index was obtained by PT. Timah, which receives the lowest CGPI index compared to other companies, both annually and on average throughout the observation period.

Table 3. Stock Liquidity

Comp	Stock Liquidity					
	2011	2012	2013	2014	2015	Avg
Aneka Tambang	0.0613	0.0548	0.0737	0.0589	0.0779	0.0653
Bank Mandiri	0.0792	0.0503	0.0751	0.0485	0.0588	0.0624
Bank Negara Indonesia	0.0737	0.0405	0.0772	0.0563	0.0719	0.0639
Bank Tabungan Negara	0.0823	0.0606	0.0802	0.0755	0.0655	0.0728
Timah	0.0802	0.0611	0.0799	0.0728	0.0762	0.0740
Bukit Asam	0.0763	0.0595	0.0789	0.0610	0.0816	0.0715
Jasa Marga	0.0578	0.0449	0.0566	0.0454	0.0568	0.0523
Average	0.0730	0.0531	0,0745	0.0598	0.0698	

The stock liquidity is measured using the bid-ask spread and the results are presented in Table 3. The bid-ask spread is a comparison between the bid price and the share price request on trading on the Stock Exchange. The greater the spread between the bid and ask shows the low level of stock liquidity. The greater value of spreads can also be interpreted as an information gap between capital market players.

When viewed as a whole, the spread value tends to fluctuate, with the lowest spread in 2012 and the highest spread in 2013. This means that the company's shares have the highest level of liquidity in 2012 and the lowest level of liquidity in the year 2013. During the observation period of 2011-2015, companies that have the highest level of liquidity are PT. Jasa Marga and the lowest are owned by PT. Timah. The highest level of stock liquidity was owned by Bank Negara Indonesia in 2012, while the lowest was at the Bank Tabungan Negara in 2011.

Table 4. Regression Result

	df	*F*	*Sig. F*
Regression	1	7,041	0,0122

Statistical test results show that there is a significant negative effect of Good Corporate Governance on stock liquidity, with a significance value of 0.012 (less than 0.05). The negative influence is caused by liquidity proxies that use bid-ask spreads which have the opposite meaning to liquidity. The higher the bid-ask spread shows the low level of liquidity and vice versa. Thus, the negative direction shows that the implementation of Good Corporate Governance will increase the level of stock liquidity. The research hypothesis which stated that Good Corporate Governance has a significant influence on stock liquidity is accepted. The coefficient of determination was conducted to measure the influence of Good Corporate Governance has on stock liquidity. R square results indicate that 42% is the influence of Good Corporate Governance on stock liquidity.

The regression formula for this research is:

LIQ = 0.103 – 0.0005 GCG + 0.014

5. DISCUSSION

The presence of significant influence from Good Corporate Governance on stock liquidity shows that the implementation of good corporate governance will have an impact on reducing the level of asymmetry information. 5 GCG principles namely accountability, responsibility, transparency, fairness, and independence will encourage companies to be more disclosure in providing information. Through disclosure, external parties will have the appropriate information in decision making, and this will increase stock liquidity. Companies with good corporate governance will have a high level of stock liquidity because good governance improves financial and operational transparency, which in turn reduces information asymmetry between management and owners.

The result is consistent with those of Chung et al [16], Ajina et al.[17], Diamond & Verrecchia [22], Barth et al. [18], Habib et al. [23], Tang & Wang [19], Lei et al [20], Levine and Zervos [24], Bekaert et al. [25] and Bekaert et al. [21], which conclude that companies with good corporate governance are likely to have liquid secondary markets for their shares because good governance improves financial and operational transparency, which ultimately reduces information asymmetries between the insiders and outside owners/liquidity providers.

6. CONCLUSIONS AND RECOMMENDATIONS

This research has a hypothesis which states that there is a significant influence of Good Corporate Governance on stock liquidity. From the results of statistical tests, it can be stated that the research hypothesis is accepted with the effect is 42%.

This research still has limitations and there are opportunities for further research to conduct similar studies as a form of scientific development. Some suggestions that can be submitted for further research are: (1) using governance mechanisms with variables such as ownership structure, the board of directors, and audit committee, (2) There is no appropriate measure for stock liquidity, thus the use of other measures such as Amihud's ratio or Liu's Model can be used as a comparison, (3) The use of a larger sample considering the companies that listed on Indonesia stock exchange has an increasing trend.

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