SUPPORTING FACTORS FOR THE SUCCESSFUL IMPLEMENTATION OF CORPORATE GOVERNANCE IN HANDICRAFT SMES

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Abstract

Purpose of Study: This research is to analyze and study factors that influence the successful implementation of good corporate governance in handicraft SMEs based on several factors related to business ethics, public information, and the company's ability to develop, be sustainable and compete. This study also aims to create a new element from several groups of factors that can be categorized based on grouping in a component matrix.

Methodology: This research was conducted using a descriptive correlational design. The samples were 54 handicraft SMEs that have implemented corporate governance principles in five regencies in West Governance. The sampling technique uses simple random sampling in 5 districts in West Java Province. Data processing used Exploratory Factor Analysis (EFA).

Main Findings: The results show that the four factors support the successful implementation of Handicraft SME’s corporate governance. The first factor is profitability, financial report integrity, and competitiveness, this primary factor is called competitiveness. The second factor is decision making, business ethics, and planning and organizing aspects, and this factor is called leadership. The third factor is sustainability and access to banking and this factor is called the bankable factor. The fourth factor consists of growth and public information, and these factors are called growth factors.

Applications of this study: The results of this study can be used as a reference by handicraft SMEs to develop business management to improve leadership factors and maintain growth so that it becomes bankable and competitive. This information is also useful for investors and financial service providers to provide capital to handicraft SMEs.

Novelty / Originality of this study: First, this research formed a new factor that supports the success of governance in handicraft SMEs; these factors are leadership, competitiveness, bankable, and growth. These four factors are the main factors determining the successful implementation of corporate governance in handicraft SMEs. Both of these studies combine several concepts from previous research the characteristics of SMEs in West Java, Indonesia.

Keywords: Corporate Governance, Competitiveness, Growth, Bankable, SMEs.

INTRODUCTION

The implementation of good corporate governance can help SMEs get alternative funding from investors and financial institutions (Gü & Apak, 2014). Corporate governance deals with the management of relationships among different parties in a company, both formal and informal. The purpose is to effectively maintain a balance between the interests of different parties in a company (Lashgari, 2004; Mudashirul & Bakare, 2014; Narwal & Jindal, 2015). The adoption of good corporate governance in a company was found to improve operational transparency, ensure accountability, and improve profitability. This also helps protect the interests of shareholders by aligning their interests with those of the managers. Generally, cooperative governance was found to have positive impacts on organizational performance (Mudashirul & Bakare, 2014; Narwal & Jindal, 2015).

Small and medium-sized enterprises (SMEs) play a considerable role in the national economy. Their contribution to GDP reached 60.34 percent. This shows how good their performance is (Hamdani & Susilawati, 2018; Hamdani, 2018). Some studies show that corporate governance was not well-implemented in SMEs in Indonesia. They were too focused on profit rather than the implementation of good governance principles (Ilvas & Rafia, 2012). There are two conflicting views on the implementation of corporate governance principles in SMEs (Abor & Adjasi, 2007). The first view sees no urgency in implementing good corporate governance because there is no agency in SMEs. There is no such thing as an owner-management mechanism usually found in big companies (Hanifah, 2015). On the other hand, there have been many pieces of evidence of the successful implementation of corporate governance in SMEs in developed countries (OECD, 2018). SMEs can learn from how big companies implement the principles of an effective governance system (Jaswadi, 2017).

SMEs are frequently constrained by capital limitation, owner’s limited education, poor competitiveness, poor management, financial access difficulties, and so on (Suyono, 2018). Several studies have shown that the implementation of corporate governance can make a company perform better. Research on the implementation of corporate governance in the country of Malaysia supervised by the role of the Malaysian Company Commission, which has the duty to ensure compliance with corporate governance standards in Malaysian state-owned SMEs. (Umrani, Johl, & Ibrahim, 2015). SMEs in African countries have implemented corporate governance so they can easily get financial access (Lekhanya, 2015).
Good corporate governance (GCG) can be implemented in SMEs to improve their management system even though GCG comes from practices of big companies where ownership and control management are separated.

LITERATURE REVIEW

Corporate governance is derived from the separation of ownership from control frequently termed as an agency. Corporate governance is required to help minimize conflicts of interests between agents and principals (Yusof, 2016; Khan, 2011). Corporate governance is a series of structured processes used to manage and direct or lead corporate businesses to improve corporate values and ensure business continuity. In short, GCG can be defined as a set of systems to govern and control a company to create added value for the stakeholders. GCG can encourage clean, transparent, and professional management (Komite Nasional Kebijakan Governance, 2006). Its implementation in a company can attract both domestic and foreign investment (Gill, Sharma, Mand, & Mathur, 2012).

The key to successful SME management and the implementation of its strategy is to design a performance management system that enables leaders in the company to monitor the implementation of the GCG framework optimally (Yacuzzi, 2005). Corporate social responsibility, risk management, transparency, internal control, and internal auditors are things SMEs take into account to deal with competition (Ateba, Ohei, Maredza, Deka, & Schutte, 2015). The strengthening of SMEs implies strengthening the country’s economy because SMEs occupy more than 90% of businesses in Indonesia (Suyono, 2018).

Some factors that encourage the implementation of corporate governance include the desire for transparency, business ethics, disclosure of SME information to the public, better management system, strong internal audit, opportunities to grow (Afande, 2015). Studies have shown that there is a positive correlation between the implementation of corporate governance and SME profitability (Afande, 2015; Mudashiri & Bakare, 2014). Corporate governance should be urgently implemented in SMEs, especially to present credible and reliable financial statements to investors or banks (Amoako, Marfo, Gyabaah, & Gyamfi, 2014). Corporate governance is required for risk management, better decision making, better principle application and better financial statement (ASX, 2006).

RESEARCH METHOD

This research was conducted using a descriptive correlational design. The samples were 54 handicraft SMEs that have implemented corporate governance principles in five regencies in West Governance. Data were analyzed using Exploratory Factor Analysis (EFA) by means of SPSS 22. EFA was conducted to figure out a new concept and the latent variable.

RESULTS AND DISCUSSION

Table 1 presents the results of KMO and Bartlett’s Test in SPSS. Using the significance level of 0.05, the suggested correlational coefficient was higher than 0.5. The MSA value was 0.584 and the significance was 0.000, meaning that further analysis process was feasible.

| KMO and Bartlett’s Test |       |
|-------------------------|-------|
| Kaiser-Meyer-Olkin Measure of Sampling Adequacy. | .584  |
| Bartlett's Test of Sphericity |       |
| df | 66 |
| Sig. | .000 |

Anti-Image Matrices in the appendix shows which variable was feasible for further analysis and which was not. The marking (*) indicates the MSA value of a variable. The MSA value of variables Business Ethics was 0.532, Transparency was 0.348, Public Information was 0.835, Planning & Organizing Aspect was 0.685, Internal Audit was 0.463, Growth was 0.568, Profitability was 0.586, Financial Report Integrity was 0.581, Decision Making was 0.556, Access to Banking was 0.619, Competitiveness was 0.694, and sustainability was 0.512. Since the MSA value of the variables
transparency and internal audit were lower than 0.5, these variables were removed and data analysis was redone without them.

Table 2: Communalities

| Table 2: Communalities | Initial | Extraction |
|------------------------|---------|------------|
| Business Ethics        | 1.000   | .779       |
| Public Information     | 1.000   | .554       |
| Planning & Organizing Aspect | 1.000 | .324       |
| Growth                 | 1.000   | .766       |
| Profitability          | 1.000   | .894       |
| Financial Report Integrity | 1.000 | .859       |
| Decision Making        | 1.000   | .635       |
| Access to Banking      | 1.000   | .753       |
| Competitiveness        | 1.000   | .714       |
| Sustainability         | 1.000   | .663       |

Extraction Method: Principal Component Analysis.

Table 2 shows that business ethics has the extraction value of 0.779, meaning that 77.9% of variance of this variable can be explained by the established factors, that planning and organizing aspect has the extraction value of 0.324, which means that 32.4% of variance of this variable can be explained by the established factors, and so forth.

Table 3: Total Variance Explained

| Table 3: Total Variance Explained | Initial Eigenvalues | Extraction Sums of Squared Loadings |
|-----------------------------------|---------------------|-------------------------------------|
| Component                         | Total               | % of Variance | Cumulative % | Total | % of Variance | Cumulative % |
| 1                                 | 3.086               | 30.862        | 30.862       | 3.086 | 30.862        | 30.862       |
| 2                                 | 1.734               | 17.341        | 48.203       | 1.734 | 17.341        | 48.203       |
| 3                                 | 1.094               | 10.939        | 59.142       | 1.094 | 10.939        | 59.142       |
| 4                                 | 1.026               | 10.263        | 69.404       | 1.026 | 10.263        | 69.404       |
| 5                                 | .895                | 8.951         | 78.356       |       |              |              |
| 6                                 | .703                | 7.026         | 85.382       |       |              |              |
| 7                                 | .673                | 6.735         | 92.117       |       |              |              |
| 8                                 | .441                | 4.406         | 96.523       |       |              |              |
| 9                                 | .317                | 3.168         | 99.691       |       |              |              |
| 10                                | .031                | .309          | 100.000      |       |              |              |

Extraction Method: Principal Component Analysis.

Table 3 shows that there were four factors established out of 10 input variables, indicated by the eigenvalues higher than 1. The eigenvalues of Factors 1-4 were 3.086, 1.734, 1.094, and 1.026 respectively. The total variance was 69.4%. The figure shows the Scree Plot which shows the relationship between established factors in the form of a graphic.

Figure 1: Scree Plot
Table 5 shows the component matrix where each of the independent variables is put in Factors 1–4.

**Table 5: Component Matrix**

| Component                          | 1    | 2   | 3    | 4   |
|------------------------------------|------|-----|------|-----|
| Profitability                      | .918 | .106| -.187| -.074|
| Financial Report Integrity         | .870 | .149| -.277| -.053|
| Competitiveness                    | .778 | .293| .098 | -.115|
| Decision Making                    | .294 | .679| .191 | .226 |
| Business Ethics                    | -.227| .593| .528 | -.309|
| Planning & Organizing Aspect       | .059 | .560| .013 | .086 |
| Sustainability                     | .349 | -.501| .425 | -.331|
| Access to Banking                  | .382 | -.305| .681 | .224 |
| Growth                             | .541 | -.310| .059 | .611 |
| Public Information                 | -.424| .219| .097 | .563 |

Extraction Method: Principal Component Analysis.

a. 4 components extracted.

The input variable depends on the correlational value between the variable and the factor. What follows is the established factors and their variables:

**Factor 1:**
1. Profitability
2. Financial Report Integrity
3. Competitiveness

**Factor 2:**
1. Decision Making
2. Business Ethics
3. Planning & Organizing Aspect

**Factor 3:**
1. Sustainability
2. Access to Banking

**Factor 4:**
1. Growth
2. Public Information

Factor 1 consisted of the variables profitability, financial report integrity, and competitiveness. Factor 1 was then called competitiveness since profitability, finance, and competitiveness are business performance establishing factors. Business performance is said to be a driving factor in the implementation of corporate governance (Hamad, 2011). The implementation of corporate governance was found to improve business performance (Arosa, Iturralde, & Maseda, 2013). Other studies showed that corporate governance had a positive influence on business performance (Hove-sibanda, Sibanda, Pooe, West, & Africa, 2013; Amoateng, Osei, Ofori, & Gyabaa, 2017). Factor 2 consisted of the variables decision making, business ethics, and planning and organizing. This factor was then named the leadership factor. This factor is established internally to encourage better SME management (Nainawat & Meena, 2013; Patrick, Paulinus, & Nymph, 2015). Factor 3 consisted of the variables sustainability and access to banking and was then called the bankable factor. Access to banking is one of the reasons for implementing corporate governance (Gill et al., 2012; Hove-sibanda et al., 2013). Factor 4 consisted of the variable’s growth and public information and was then called a growth factor. Credibility is very important for creating quality, capability and for obtaining public trust. Credibility is the key to the success of SMEs in Thailand (Chittithaworn, Islam, Hasliza, & Yusuf, 2011).

**CONCLUSION**

Four factors were encouraging the implementation of good corporate governance in handicraft SMEs in West Java. The reasons for the implementation of good corporate governance were to improve business performance, to prepare better business planning, to gain banking access, and to improve growth and to disclose information to the public. Based on this reasoning, it can be concluded that the four factors were business performance, management, accessibility, and credibility.

**LIMITATION AND STUDY FORWARD**

This study only analyzes the supporting factors for the successful implementation of Handicraft SMEs based on several concepts without connecting with the business performance of SMEs Handicraft. Another limitation is the relatively small number of samples of 54 HandicraftsSME. Future research should also examine the linkages of governance with SME business performance, and the number of samples should represent each region in the province of West Java. Future research that leads to digital business, with the 4.0 Revolution changing the way in doing business, so this is important in the future to be studied.
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Appendix: Anti-Image Matrices

| Anti-image Matrices | Business Ethics | Transparency | Public Information | Plannin g & Organizing Aspect | Internal Audit | Growth | Profitability | Financial Report Integrity | Decision Making | Access to Banking | Competitiveness | Sustainability |
|---------------------|----------------|-------------|-------------------|-----------------------------|----------------|--------|--------------|---------------------------|-----------------|-----------------|---------------|---------------|
| Business Ethics     | .690           | -.129       | -.011             | -.053                       | -.138          | .260   | -.010        | -.007                      | -.165           | -.141           | -.001         | -.027         |
| Transparency        | -.129          | .815        | -.136             | -.112                       | -.067          | .054   | -.053        | .048                       | -.120           | .042            | .106          | -.044         |
| Public Information  | -.011          | .820        | .074              | .114                        | -.003          | .012   | .001         | -.024                      | .008            | .004            | .080          |               |
| Planning & Organizing Aspect | -.053          | -.112       | .074              | .867                        | .084           | -.025  | .010         | -.004                      | -.056           | .063            | -.088         | .070          |
| Internal Audit      | .138           | -.067       | .114              | .084                        | .657           | .195   | .020         | -.037                      | -.017           | -.028           | .070          | -.258         |
| Growth              | .260           | .054        | -.003             | -.025                       | .195           | .594   | -.011        | -.006                      | -.125           | .211            | .063          | -.122         |
| Profitability       | .010           | -.053       | .012              | .010                        | .020           | -.011  | .052         | -.053                      | .027            | -.029           | -.059         | -.037         |
| Financial Report Integrity | -.007          | .048        | .001              | -.004                       | -.037          | -.006  | -.053        | .062                       | -.026           | .030            | .033          | .054          |
| Decision Making     | -.165          | -.120       | -.024             | -.056                       | -.017          | -.125  | .027         | -.026                      | .677            | .037            | -.196         | .119          |
| Access to Banking   | -.141          | .042        | .008              | .063                        | -.028          | -.211  | -.029        | .030                       | .037            | .776            | -.007         | -.078         |
| Competitiveness     | -.001          | .106        | .004              | -.088                       | .070           | .063   | -.059        | .033                       | -.196           | -.007           | .393          | -.117         |
| Sustainability      | -.027          | -.044       | .080              | .070                        | -.258          | -.122  | .037         | .054                       | .119            | -.078           | -.117         | .584          |
### Anti-image Matrices

|                        | Business Ethics | Transparency | Public Information | Planning & Organizing Aspect | Internal Audit | Growth | Profitability | Financial Report Integrity | Decision Making | Access to Banking | Competitiveness | Sustainability |
|------------------------|-----------------|--------------|--------------------|-------------------------------|----------------|--------|--------------|-----------------------------|----------------|-----------------|-----------------|----------------|
| Business Ethics        | .532<sup>a</sup> | -.172        | -.015              | -.068                         | .205           | .405   | .051         | -.036                        | -.241          | -.193           | -.002           | -.043          |
| Transparency           | -.172           | .348<sup>a</sup> | -.166              | -.133                         | -.091          | .077   | -.260        | .215                         | -.161          | .053            | .187            | -.064          |
| Public Information     | -.015           | -.166        | .835<sup>a</sup>   | .088                          | .156           | -.005  | .058         | .006                         | -.032          | .010            | .006            | .115           |
| Planning & Organizing  | -.068           | -.133        | .088               | .685<sup>a</sup>              | .112           | -.035  | .045         | -.019                        | -.073          | .077            | -.151           | .098           |
| Aspect                 |                 |              |                    |                               |                |        |              |                              |                |                 |                 |                |
| Internal Audit         | .205            | -.091        | .156               | .112                          | .463<sup>a</sup> | .313   | .110         | -.184                        | -.026          | -.040           | .138            | -.416          |
| Growth                 | .405            | .077         | -.005              | -.035                         | .313           | .568<sup>a</sup> | -.060 | -.034        | -.197                        | -.311          | .130            | -.208           |                |
| Profitability          | .051            | -.260        | .058               | .045                          | .110           | -.060  | .586<sup>a</sup> | -.940                        | .147           | -.143           | -.414           | -.210          |
| Financial Report       | -.036           | .215         | .006               | -.019                         | -.184          | -.034  | -.940        | .581<sup>a</sup>             | -.128          | .136            | .213            | .287           |
| Integrity              |                 |              |                    |                               |                |        |              |                              |                |                 |                 |                |
| Decision Making        | -.241           | -.161        | -.032              | -.073                         | -.026          | -.197  | .147         | -.128                        | .556<sup>a</sup> | .052            | -.379           | .189           |
| Access to Banking      | -.193           | .053         | .010               | .077                          | -.040          | -.311  | .143         | .136                         | .052           | .619<sup>a</sup> | -.014           | -.116          |
| Competitiveness        | -.002           | .187         | .006               | -.151                         | .138           | .130   | -.414        | .213                         | -.379          | -.014           | .694<sup>a</sup> | -.244          |
| Sustainability         | -.043           | -.064        | .115               | -.098                         | -.416          | -.208  | -.210        | .287                         | .189           | -.116           | -.244           | .512<sup>a</sup>|

<sup>a</sup> Measures of Sampling Adequacy (MSA)