

# Chapter I

## Introduction

### 1.1 Background

Bank Century bailout case is one of the many news attract people of Indonesia for the last few years. The case of Bank Century begins with maturities of marketable securities of Century Bank's property worth US \$ 56 million and eventually defaulted. From Bank Century events that led to liquidity problems. The liquidity problems continue in clearing or failure cannot be pay funds by Bank Century customers demand caused by failing to provide funds (prefund) resulting in the withdrawal of funds customer massively (rush). Bank Indonesia as central bank establishes Bank Century as a failed bank that hedge systematic and require further treatment. (www.ikatanbankir.com, March 2015).

The experience of such cases encourages the need for new regulations in banking. Innovation in products, services and banking activities that do not offset by the application of adequate risk management can raises fundamental problems at the bank. Banks need to improve the effectiveness of risk management and good corporate governance intended that the bank can identify problems early and can conduct appropriate follow-up improvements and faster so the banks more resilient in the face of crisis (Circular Letter of Bank Indonesia No. 15/15 / DPNP / 2013).

In accordance with Act No. 10 of 1998 that bank as financial intermediary that collecting funds from the public and to channel it back to community in the form of credit. Banks should maintain confidence given the community in

managing their funds. An embodiment of seriousness of banks in managing public funds is to maintain health performance, because the bank rating is very important for business institutions. Then, bank management will follow-up all of requirement to maintain the bank health and it can resulted into public confidence.

Both healthy and unhealthy bank is very hard to be distinguished seen from their balance sheet. According to Heffernan (2005:462) it begins with the need to distinguish insolvent from illiquid banks. In practice, the boundary between the two can be fickle and unclear. The increased complexity of bank balance sheets can make it difficult to distinguish between the two. Many troubled banks, on the brink of failure, will have assets with a total “real” value (as quantified post-crisis) exceeding liabilities, even though this may well not be the case at the height of the panic. Furthermore, studies such as James (1991) have shown that liquidating insolvent banks is more costly than restructuring them, through, for example, a bailout or merger with a healthy bank, or (nationalization). This may explain why Goodhart and Schoenmaker (1995) found that out of 104 failing banks (in 24 countries), 73 were rescued and the other 31 liquidated. Santomero and Hoffman (1998) report that even though banks had poor CAMEL ratings, they were given access to the Fed’s discount window between 1985 and 1991. Therefore, the need of international financial architecture is really needed. The objectives are to design a global financial structure, and a means of regulating and coordinating institutions within that structure, to minimize the probability of a major financial crisis occurring. Also, to have in place methods for dealing with a crisis, should it occur (Heffernan, 2005).

The benefits of this research to clients and investors are as consideration for customers and investors in decision-making in choosing a bank. By choosing a healthy bank will hopefully avoid risks-risks that bank often faced. This assessment aims to determine whether the bank is included in the bank's condition healthy or unhealthy banks views of the risk profile, good corporate governance, earning ratios and capital. Banks that get the predicate healthy bank obliged to maintain its health. For banks that are included in unhealthy bank, then the Board of Directors, Board of Commissioners, and/or controlling shareholder is obligated to deliver action plan to Bank Indonesia (Bank Indonesia Regulation No. 13/1/PBI/2011).

This research is still needed at the moment because in investing neither the investor's funds nor the customer will certainly prefer the banks included in the healthy category. Banks whose rating is increasing from year to year will certainly attract more investors as well as customers. Unhealthy banks, not only harm itself, but also other parties. Bank rating is very important because the bank manages funds of the community entrusted to the bank. The community fund as the owner can only withdraw funds at any time and the bank should be able to restore the funds that went to remain trusted by customers. Therefore, if the community is going to draw their money in massively, it could trigger the one of the biggest problems in banking. It is problem of liquidity for banks, which further can lead to bankruptcy of banks. The repair of the banking system must be made to foster public confidence back against the national banking.

Dynamic changes of bank rating system development, it is expected that the bank health should reflect the condition of the bank today and in the future. Hence,

the Bank Performance should be perfectly developed. This research method is using Risk-Based Bank Rating (RBBR), namely the assessment of the level of health risk approach by using a bank. The assessment is done, when the comprehensive analysis on performance, risk profile, problems encountered, and the prospect of the development of bank (PBI No. 13/1/PBI/2011)

Bank Indonesia Regulation No. 6/10/PBI/2004 with its assessment factor classified into six factors called CAMELS (Capital, Asset Quality, Management, Earnings, Liquidity, and Sensitivity to Market Risks). The legal basis of bank rating by Bank Indonesia Regulation No. 13/1/PBI/2011 on January 5, 2011 that replace Bank Indonesia Regulation No. 6/10/PBI/2004 has been in effect for seven years. Technical manual implementation refers to Circular Letter of Bank Indonesia No. 13/24/DPNP on October 25, 2011, the banks are required to conduct self-assessment of the bank by using a risk approach (Risk-based Bank Ratings / RBBR) either individually or as consolidation, with coverage factors include assessment of the risk profile, good corporate governance (GCG), profitability, and capital to produce a composite rating of bank rating.

The object of this research are banking companies published the financial statements and are registered with Indonesian Stock Exchange during the period 2013-2015. Reason the selection of the research object because the bank had a good management in managing the business also they had many bank customers in across business sectors. Based on the explanation on this study intends to resolve the issue of research, namely “National Private Bank Performance Analysis using Risk-Based Bank Rating Method (Case Study for PT. Bank Central Asia Tbk., and PT. Bank CIMB Niaga Tbk.)”.

## 1.2 Problem Formulation

Based on the background, identification, and restrictions on the problem above, the main problems in this study can be formulated:

1. How is the Bank Performance based on risk profile criteria during the period 2013-2015 in accordance with Circular Letter of Bank Indonesia?
2. How is the Bank Performance based on good corporate governance criteria during the period 2013-2015 in accordance with Circular Letter of Bank Indonesia?
3. How is the Bank Performance based on earnings criteria during the period 2013-2015 in accordance with Circular Letter of Bank Indonesia?
4. How is the Bank Performance based on capital criteria during the period 2013-2015 in accordance with Circular Letter of Bank Indonesia?
5. How is the overall bank rating during the period 2013-2015 in accordance with Circular Letter of Bank Indonesia?

## 1.3 Research Objectives

This study has the objective:

1. To determine the Bank Performance based on risk profile during period 2013-2015 in accordance with the Circular Letter of Bank Indonesia.
2. To determine the Bank Performance based on good corporate governance during period 2013-2015 in accordance with the Circular Letter of Bank Indonesia.



3. To determine the Bank Performance based on the earnings during period 2013-2015 in accordance with the Circular Letter of Bank Indonesia.
4. To determine the Bank Performance based on capital during 2013-2015 in accordance with Circular Letter of Bank Indonesia.
5. To determine the overall bank rating during period 2013-2015 according to Circular Letter of Bank Indonesia.

#### 1.4 Research Benefits

The benefits of this research are:

1. Academics

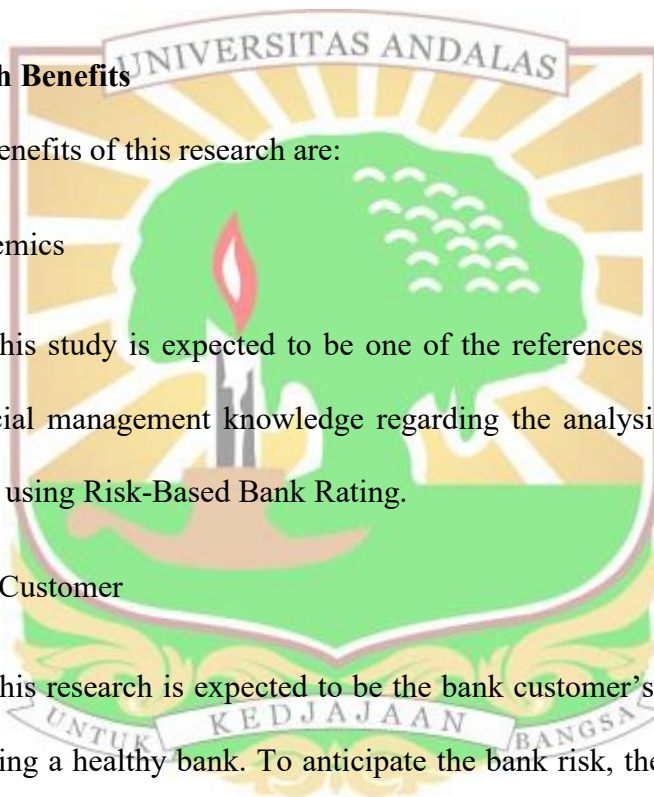
This study is expected to be one of the references developments of financial management knowledge regarding the analysis level health of banks using Risk-Based Bank Rating.

2. Bank Customer

This research is expected to be the bank customer's consideration in choosing a healthy bank. To anticipate the bank risk, the healthy bank is truly recommended.

3. Investors

This study is expected to be taken into investor's consideration who will invest their funds in the bank. By choosing a healthy bank, the investment can be growth bigger in the future.



#### 4. Bank Management

This research is expected to be considered by bank management in order to improve its performance so that the healthy predicate can be achieved. Hence, it also results for public confidence to save their money in bank and attract more potential investor to invest their money into the bank

