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Risk Management and Good Corporate Governance in Strengthening Indonesian Banking Performance

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Abstract

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This study aims to analyze the impact of risk management practices and Good Corporate Governance (GCG) implementation on the performance of the banking sector in Indonesia. The research background is rooted in the strategic role of banks in supporting national economic development while simultaneously facing various challenges such as credit, market, liquidity, operational, and cyber risks in the era of digitalization. The research method employed is a library study complemented by secondary data obtained from the financial statements of banks listed on the Indonesia Stock Exchange. The findings reveal that risk management significantly contributes to maintaining asset quality, reducing the level of Non-Performing Loans (NPLs), and improving financial performance efficiency. Meanwhile, GCG implementation strengthens transparency, accountability, and social legitimacy, although its effect on financial performance is not consistently significant across all banks. The differing results suggest that GCG practices in some institutions remain largely formalities with limited impact on performance. This study concludes that integrating risk management and GCG is a crucial strategy to strengthen the competitiveness of Indonesian banking amid global economic uncertainties.

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1. Introduction

The banking sector has a strategic role in supporting the economy of a country, including Indonesia. According to Law Number 7 of 1992 concerning Banking which was later updated through Law Number 10 of 1998, a bank is defined as a financial institution that collects funds from the public in the form of deposits and redistributes them in the form of credit and other forms in order to improve the standard of living of many people. Thus, the main role of banks is not only as a financial intermediation institution, but also as an instrument of national development that supports economic growth, financial stability, and the improvement of social welfare. The contribution of the financial sector, especially the banking subsector, can be seen from its capacity to provide access to funding, drive investment, and support a reliable and efficient payment system.

Banking functions that include raising funds, distributing credit, and providing payment system services make banks an important pillar in maintaining monetary stability. Through interest rate mechanisms, credit policies, and liquidity distribution, banks play a role in controlling inflation and maintaining macroeconomic stability. In addition, the banking subsector also has a strategic position on the Indonesia Stock Exchange (IDX), where banking stocks are often the main choice of investors because they are considered to have strong fundamentals and long-term growth prospects (Rachmawati & Sulbahri, 2023).

However, in carrying out its role, the banking industry faces a variety of complex challenges. Credit risk, market risk, liquidity risk, and operational risk are threats that must be managed properly. The phenomenon of Non-Performing Loans

(NPLs), global financial market volatility, and cyber risk threats require the implementation of comprehensive risk management. Regulations such as POJK No. 18/POJK.03/2016 concerning the Implementation of Risk Management for Commercial Banks and the Internal Capital Adequacy Assessment Process (ICAAP) approach are efforts by regulators to strengthen the foundation of risk management in the Indonesian banking sector (Sari et al., 2022).

The application of risk management is closely related to the framework known as the Risk Management Framework (RMF), where the concept of Three Lines of Defense, namely the first line of defense by business units, the second line by risk management and compliance, and the third line by internal auditors is a reference in banking industry practices. The effectiveness of risk management has been proven to significantly affect the performance of banks. Banks that are able to identify, measure, monitor, and control risks appropriately generally have a better level of financial health, both in terms of profitability and stability (Sadiyah, 2024).

In addition to risk management, another aspect that is no less important is the implementation of Good Corporate Governance (GCG). GCG principles, which include transparency, accountability, accountability, independence, and fairness, are the foundation for the creation of public trust and the sustainability of the banking business. The role of corporate organs such as the Board of Commissioners, the Board of Directors, the Audit Committee, and the Auditor is crucial in ensuring that the application of these principles runs consistently. Empirical studies show that strong GCG is able to minimize financial and nonfinancial risks, including reputational risks that can erode public trust in the banking industry (Baihaki et al., 2024).

Nevertheless, there are still research gaps that are interesting to study. Some studies have found that the application of GCG has a positive effect on banking performance, while other studies show different results (Sparta, 2020). This shows that the implementation of GCG in Indonesia is often still limited to administrative formalities and has not been fully effective in improving banking performance. Therefore, further research on the linkage between risk management and GCG on banking performance in Indonesia is very relevant and urgent to be carried out.

Based on this description, this study aims to examine the extent to which the implementation of risk management affects bank performance and assess the role of GCG in strengthening banking stability and performance. With a focus on banks listed on the Indonesia Stock Exchange, this research is expected to make an empirical as well as practical contribution in strengthening the resilience of Indonesia's banking sector amid uncertain global economic dynamics.

2. Literature Review

2.1. Risk Management in the Banking Industry

Risk management is a fundamental component in maintaining the sustainability of the banking industry which operates in an environment full of uncertainty. Credit risk, market risk, liquidity risk, and operational risk are the main focus in banking practices because they have a direct impact on financial stability and business sustainability. In Indonesia, the implementation of Risk Based Bank

Rating (RBBR) is one of the supervisory instruments used to assess the health level of banks through indicators such as Non-Performing Loans (NPL), Loan to Deposit Ratio (LDR), and Good Corporate Governance (GCG). RBBR helps banks measure the level of risk they face and adjust their business strategies to stay aligned with their existing risk management capacity. Muuna and Bawono's (2024) research shows that banks' ability to manage credit and other financial risks has been proven to play a role in improving asset quality and financial performance efficiency, which ultimately contributes to increased profitability and long-term stability.

In addition, research related to the merger of Bank Syariah Indonesia (BSI) confirms that the implementation of RBBR and the strengthening of the risk management system have a significant impact on improving the health of banks after the merger is carried out. These findings indicate that risk management practices are not only regulatory obligations, but strategic instruments to strengthen the competitiveness of national banks in the midst of global dynamics (Putra, 2023). Therefore, risk management is a key factor in creating Indonesian banking resilience, as well as determining investor confidence and the stability of the national financial system.

2.2. Good Corporate Governance (GCG) and Its Role

Good Corporate Governance (GCG) is a corporate governance principle that aims to create transparency, accountability, independence, accountability, and fairness in carrying out business operations. In the banking industry, the implementation of GCG is not only about regulatory compliance, but also a strategic instrument to strengthen public reputation and trust. The research of Salehi et al.

(2023) emphasizes the importance of the role of supervisory bodies, especially the Audit Committee, in increasing the transparency and accountability of financial statements. This role is very crucial considering that banking is a sector with a high risk of fraudulent practices, manipulation of financial statements, and potential crisis of trust.

In addition to the internal accountability aspect, GCG is also closely related to the form of social accountability. In the context of Islamic banking, the integration of GCG with Islamic Social Reporting (ISR) is part of the roadmap for the development of Indonesian Islamic banking. The study conducted by Dosinta and Yunita (2024) emphasized that the success of the roadmap is highly determined by the consistency of the application of GCG principles that support social accountability as well as business sustainability. This shows that GCG not only serves to reduce financial risks, but also becomes an important mechanism in building public trust in banking institutions. Thus, GCG serves a dual function: as an internal control mechanism and as an external strategy to strengthen the social legitimacy of banking in Indonesia.

2.3. The Relationship between Risk Management, GCG, and Banking Performance

The relationship between the implementation of risk management, GCG, and banking performance is still a topic that has given rise to academic debate. Some studies confirm a positive relationship between the two to profitability and banking stability, while others show different results. Hamdillah and Ermawati (2024), for example, found that GCG variables do not have a significant effect on banking resilience in Indonesia. These findings are in contrast to a number of studies that argue that the application of GCG principles can strengthen financial performance by improving risk management efficiency and information transparency. This gap indicates that there are variations in the implementation of GCG which may be just an administrative formality with no real impact on bank performance.

On the other hand, a study conducted by Kubota and Suryaputri (2023) provides empirical evidence that the integration of risk management with the implementation of GCG is able to increase company value, especially in Islamic banking. This shows that the effectiveness of GCG is highly determined by the consistency of implementation and management's commitment in linking it to the risk management system. Thus, despite contradictory research results, in general the literature shows that the combination of risk management and GCG has great potential in increasing stability, profitability, and investor confidence in the banking sector. This is why further research on the relationship between the two is important, in order to strengthen the empirical foundation in the context of Indonesian banking.

3. Methods

This research uses a library research approach by utilizing various relevant academic sources, especially scientific articles published and Available, official reports of financial supervisory institutions, and literature related to risk management and Good Corporate Governance (GCG) in the banking industry in Indonesia. The literature study was chosen because the topic of this research focuses on conceptualization, comparison of previous research results, and an in-depth understanding of banking governance regulations and practices in Indonesia. Through this approach, researchers can analyze the extent to which existing theories and practices support each other or even show differences in outcomes in relation to banking performance.

In addition, this study also adds empirical information obtained from the annual financial statements and sustainability reports of banks listed on the Indonesia Stock Exchange (IDX). This secondary data is considered important to enrich the analysis, because the financial statements reflect the actual condition of the bank's performance, both in terms of profitability, liquidity, and solvency. Meanwhile, the sustainability report and corporate governance report provide an overview of the extent to which banks have consistently applied risk management and GCG principles. By combining secondary data from public companies and the findings of a literature study, this study is expected to produce a comprehensive analysis that is relevant to industry practice.

The research process is carried out through several stages. First, the researcher identified literature related to risk management, GCG, and banking performance from academic databases such as Google Scholar, as well as reputable national and international journals. Second, a literature selection was carried out based on the criteria of up-to-date, relevance to the Indonesian banking context, and suitability with the research objectives. Third, the selected literature is critically analyzed to find patterns, research gaps, and consistency of findings between one study and another.

Furthermore, the bank's financial statement data is used to compare theoretical findings with actual conditions in the field.

The analysis method used is descriptive-qualitative analysis, where the results of literature processing and secondary data are described systematically. This approach allows researchers to assess the relationship between the application of risk management and GCG and banking performance from both theoretical and empirical perspectives. With this method, the research not only presents a summary of the existing literature, but also offers a new synthesis that can be the basis for further research in the future.

4. Results

The banking industry in Indonesia plays a vital role in maintaining national economic stability, as well as functioning as a driving force for economic growth. As an intermediary institution, banks collect public funds through various deposit instruments and redistribute them in the form of credit. This intermediation process not only provides benefits for banks, but also supports the productivity of the community and the business world. However, as the complexity of financial activities grows, banks also face various risks that must be managed properly. Therefore, the analysis of the results of this study focuses on the relationship between risk management, Good Corporate Governance (GCG), and banking performance in Indonesia.

One of the key findings shows that the implementation of risk management has a significant influence on banking resilience in Indonesia. Effective risk management allows banks to identify, measure, monitor, and control risks arising from intermediation activities. Research by Indraswari et al. (2024) confirms that credit risk management and other financial risks contribute directly to improving the efficiency of financial performance. Banks that are able to maintain asset quality and minimize the level of Non-Performing Loans (NPLs) will have a healthier financial structure, so that they can maintain profitability despite economic volatility. This proves that the ability to manage risk is a prerequisite for banks to maintain competitiveness in the midst of changes in the global financial market.

The implementation of the Risk Based Bank Rating (RBBR) framework introduced by regulators is an important instrument in measuring the level of banking health. Rachmawati and Sulbahri's (2023) study on Bank Syariah Indonesia (BSI) before and after the merger shows that RBBR-based risk management is able to provide a comprehensive picture of the bank's financial condition. Post-merger, the implementation of indicators such as NPL and Loan to Deposit Ratio (LDR) has succeeded in improving the health of banks. This emphasizes that the implementation of risk management regulations is not only administrative, but has a real impact in strengthening the resilience of banking institutions.

In addition to risk management, this study also highlights the importance of implementing Good Corporate Governance (GCG) in strengthening the foundation of the banking industry. The GCG principles of transparency, accountability, accountability, independence, and fairness are designed to ensure that every strategic decision of the bank is carried out ethically and in accordance with the interests of all stakeholders. According to Salehi et al. (2023), one of the important organs in

GCG is the Audit Committee, which functions to improve the quality of transparency and accountability of bank financial statements. With strong supervision from the Audit Committee, the possibility of manipulation of financial statements can be minimized, so that the level of public trust in banks increases.

Furthermore, the application of GCG in Indonesian Islamic banking is also closely related to Islamic Social Reporting (ISR). A study conducted by Khasanah (2020) shows that Indonesia's Islamic banking development roadmap 2020-2024 emphasizes the integration between GCG principles and social reporting. This not only increases the bank's legitimacy in the eyes of the public, but also strengthens business sustainability. This integration reflects that GCG is not only a tool for regulatory compliance, but also a strategy in building trust and reputation in the era of global competition. The relationship between risk management, GCG, and bank performance is not always consistent. Some studies found a significant effect, while others showed different results. Research by Hamdillah and Ermawati (2024), for example, found that GCG variables do not have a significant effect on banking resilience. These findings raise questions about the consistency of GCG implementation in Indonesia's banking sector, which in some cases is still considered to be an administrative formality with no real impact on financial performance.

On the other hand, research by Kubota and Suryaputri (2023) shows that the implementation of GCG integrated with risk management is able to increase company value, especially in the Islamic banking sector. These results emphasize that the effectiveness of GCG is highly dependent on the quality of implementation, not just the existence of formal rules. When GCG principles are applied consistently, the impact is evident in increasing profitability, company value, and investor confidence. Thus, the difference in research results shows that the main challenge is not the GCG concept itself, but the level of implementation in each bank.

The results of the analysis of the financial statements of banks listed on the IDX support the findings of the previous literature. In general, banks with low NPL ratios and maintained liquidity levels show more stable financial performance. For example, the annual reports of several major banks note that declining NPLs consistently contribute to increased Return on Assets (ROA) and Return on Equity (ROE). This is in line with the results of Sadiyah's (2024) research which emphasizes the importance of credit risk control as the main factor for improving performance. In addition, the bank's sustainability report also shows that the implementation of GCG as a whole is related to improving the company's image. Several banks that emphasize transparency in sustainability reporting have received a positive response from investors and the public. These findings support the research of Harahap and Ritonga (2024), which emphasizes that the transparency of financial statements is an important indicator in assessing the effectiveness of GCG.

Regulations from the Financial Services Authority (OJK) and Bank Indonesia play an important role in directing the implementation of risk management and GCG in national banks. Regulations such as POJK No. 18/POJK.03/2016 concerning the Implementation of Risk Management and the Internal Capital Adequacy Assessment Process (ICAAP) framework are the legal basis for banks in developing risk management strategies. Sari et al. (2022) emphasized that the implementation of a risk management framework in accordance with regulations can help banks minimize losses and increase public trust. However, the big challenge faced is how banks can implement these regulations consistently and not just limited to formalities.

In addition to traditional risks such as credit and liquidity, banks also face new risks in the form of cyber risks along with the digitalization of banking services. This risk demands an update of risk management policies and an increase in information technology capacity. Some digital banks in Indonesia have begun to emphasize this aspect in their reports, but the gap in the implementation of cybersecurity standards is still a crucial issue that needs attention. The results of this study show that effective risk management and consistent implementation of GCG have a positive influence on banking performance in Indonesia. However, there are differences in the effectiveness of GCG implementation in various banks, which is often determined by management's commitment to implementing governance principles. Risk management has proven to be more consistent in having a positive impact, especially in maintaining asset quality, lowering NPL levels, and strengthening financial stability. On the other hand, GCG still faces implementation challenges that cause its impact on performance to be not uniform across all banking institutions.

Thus, it can be concluded that the success of the Indonesian banking industry in facing global challenges is not only determined by regulations, but also by the extent to which banks are able to internalize the principles of risk management and GCG into the organizational culture. Consistent implementation, support from internal supervisory bodies, and compliance with external regulations are key factors in improving banking performance and resilience.

5. Discussion

The results of the study show that risk management and Good Corporate Governance (GCG) are two important aspects that complement each other in strengthening the performance of Indonesian banks. In terms of risk management, the findings confirm that credit risk control, liquidity, and markets make a significant contribution to the bank's profitability and financial stability. The study of Muuna and Bawono (2024) emphasizes that banks that manage to maintain asset quality and reduce Non-Performing Loans (NPL) numbers show more efficient performance, both in terms of Return on Assets (ROA) and Return on Equity (ROE). Thus, risk management can be seen as an internal mechanism that directly impacts the bank's financial indicators.

However, the implementation of GCG provides a broader perspective because it concerns not only financial efficiency, but also aspects of public trust, reputation, and social legitimacy. Harahap and Ritonga (2024) emphasized that the existence of an Audit Committee and the transparency of financial statements are important elements in strengthening investor confidence. On the other hand, the integration of GCG with Islamic Social Reporting (ISR) in Islamic banking as highlighted by Dosinta and Yunita (2024) shows that good governance can also be a strategic instrument in building long-term relationships with the community. This means that GCG functions not only as a regulatory tool, but also as a reputation strategy that supports business sustainability.

The difference in research results regarding the influence of GCG on bank performance is an interesting issue that needs to be examined more deeply. The contradictory results of the study, as revealed by Fadhlilhaq et al. (2024), indicate that not all banks are able to apply GCG principles consistently. In some cases, GCG is still an administrative formality that does not have a real impact on financial performance. This shows that there is a gap between regulation and implementation in the field. Therefore, further research is needed to identify the factors that affect the effectiveness of GCG implementation, including management commitment, organizational culture, and internal oversight systems. In addition, the new challenges facing the banking sector in the form of digital risks and cybersecurity demand the integration of risk management and GCG in a more adaptive framework. Banks need to develop risk policies that are able to anticipate technological threats while ensuring that corporate governance supports transparency and accountability in dealing with these risks.

This is becoming increasingly important in the midst of the rapid digital transformation of banking in Indonesia. Thus, this discussion emphasized that the success of the Indonesian banking industry in maintaining stability and improving performance is not only determined by existing regulations, but also by the consistency of the implementation of risk management and GCG principles. The combination of the two can form a complementary system: risk management maintains the financial health of banks, while GCG strengthens public legitimacy and trust. This synergy will ultimately strengthen the competitiveness of Indonesian banks in facing global economic dynamics.

6. Conclusion

This research confirms that risk management and Good Corporate Governance (GCG) have a strategic role in strengthening banking stability and performance in Indonesia. Effective risk management allows banks to identify and control credit, market, liquidity, and operational risks, thereby maintaining asset quality and increasing profitability. Meanwhile, the consistent implementation of GCG strengthens public trust through transparency, accountability, and integrity governance. However, the research also found that the implementation of GCG in some banks is still a formality so that the impact on performance is not always consistent. This shows that there is a gap between regulation and practice in the field, which needs special attention from banking management and regulators.

In addition, new challenges in the form of digitalization and cyber risk require innovation in risk management and GCG adaptation to suit the context of technological transformation. This research emphasizes the importance of integration between risk management and GCG as a holistic strategy to strengthen the competitiveness of Indonesian banks. With consistent and sustainability-oriented implementation, the banking sector will not only be more resilient to global dynamics, but also able to make a significant contribution to national economic development.

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