

THE PATTERN OF STRATEGY AND ORGANISATION STRUCTURE AFFECTING THE CORPORATE GOVERNANCE OF BANK IN INDONESIA

Muhammad Akbar

Doctoral Program in Business Management Faculty of Economy and Business

Padjajaran University, Bandung, Indonesia

E-mail: makb1234@yahoo.com

ABSTRAK: Saat ini terdapat beberapa praktek tata kelola perusahaan yang dikenal luas dalam konteks ekonomi global, khususnya di perusahaan jasa seperti perbankan. Setelah Krisis Keuangan Asia melanda, negara-negara di Asia mulai melakukan reformasi terhadap praktek tata kelola perusahaan. Tujuan penelitian ini: (1) untuk membahas pengaruh pola strategi dan struktur organisasi terhadap tata kelola perusahaan dengan menggunakan data perbankan di Indonesia, (2) membahas perbedaan spesifik (*missing link*) terkait hubungan antara pola strategi dan struktur organisasi serta dampaknya terhadap tata kelola perusahaan. Metode yang digunakan adalah metode kuantitatif deskriptif dan dengan *semi structured interview*. Dapat disimpulkan bahwa: (1) pola strategi dan struktur organisasi sangat menentukan penerapan tata kelola perusahaan, dimana bukan hanya faktor *realized strategy* yang harus diperhatikan tapi juga *intended strategy*, (2) *missing link* tersebut adalah strategi dan struktur organisasi yang tepat yang dapat dikombinasikan bersama untuk meningkatkan pemahaman dan *awareness* perusahaan tentang tata kelola perusahaan yang baik dalam rangka memperbaiki kinerja bank, melindungi kepentingan pemangku kepentingan dan meningkatkan kepatuhan terhadap peraturan dan kode etik umum yang berlaku di industri perbankan.

Kata Kunci: tata kelola perusahaan, strategi perusahaan, struktur organisasi, pola strategi, bank, indonesia

ABSTRACT: *The increasingly recognized premium for good corporate governance is considered in the context of a globalizing economy, especially in service organisations, such as banks. After the Asian Financial Crisis, all the Asian countries have embarked on reform of corporate governance. The aim of this research is: (1) to investigate the influences of pattern of strategy and organisation structure to the Corporate Governance using Indonesian banking data, and (2) to investigate whether there is a distinct lack of research into the relationship between pattern of strategy and organisation structure and its impact to corporate governance. The research method used is quantitative method and semi-structured interview. The conclusions are: (1) pattern of strategy and organization structure have significant impact to the implementation of good corporate governance, which is not only realized strategy as the main factor but also need to pay attention to the intended strategy, (2) this kind of missing an appropriate strategy and organisation structure can be combined together to have a good awareness and understanding about corporate governance to improve bank performance, protect stakeholders' interests and increase compliance to prevailing regulations and general code of conduct in the banking industry.*

Keywords: corporate governance, corporate strategy, organisation structure, patterns of strategy, bank, Indonesia

INTRODUCTION

The background of the research is that after the Asian Financial Crisis, all the Asian countries have embarked on reform of corporate governance and many industrial players ask whether a universal corporate governance system is either necessary or desirable. The increasingly recognized premium for good corporate governance is considered in the context of a globalizing economy. Financial institutions, in particular banks, have come under increasing pressure, since the sub-prime mortgage crisis and the following credit crunch to take a more long-term view of their investors' business interests and to acknowledge and respond to their obligations to society (Matten 2006; Money and Schepers 2007; Gill 2008; Grove *et al.* 2011).

According to Thomas (2007), that the future direction of corporate governance trends is

questioned, with likelihood greater complexity rather than uniformity emerging from current development.

In facts, within the Asian countries, Indonesia just introduce corporate governance code in 2001 and for banking industry is 2006. Bank Indonesia for the first time issued Bank Indonesia Regulation No. 8/4/PBI/2006 dated January 30, 2006 considering the following factors: (a) increasing risk complexity faced by banks, (b) in order to improve Bank performance, protect stakeholders' interests and increase compliance to prevailing regulations and general code of conduct in the banking industry.

Some banks just taking into account as "obligation" than "need". So that the implementation just focus to the strategy to complete organisation structure as it is without looking at the pattern of strategy and appropriate organization structure to support good corporate governance.

On the other hand, after more than 30 years of hard thinking about strategy, consultants and scholars have provided an abundance of framework for analyzing strategic situations. Missing, however, has been any guidance as to what the product of these tools should be-or what actually constitutes a strategy. Strategy has become a catchall term used to mean whatever one wants it to mean. Executives now talk about their “service strategy,” their “branding strategy,” their “acquisition strategy” or whatever kind of strategy that is on their mind at a particular moment (Hambrick and James, 2001). This kind of missing an appropriate of pattern of strategy and organization structure can be combined together to have a good awareness and understanding about corporate governance to improve bank performance, protect stakeholders’ interests and increase compliance to prevailing regulations and general code of conduct in the banking industry.

The aim of this research is to (1) to investigate the influences of pattern of strategy and organisation structure to the Corporate Governance using Indonesian banking data, and (2) to investigate whether there is a distinct lack of research into the relationship between pattern of strategy and organisation structure and its impact to corporate governance.

RESEARCH METHODOLOGY

In this part, the statistical procedures will be applied in order to answer the question regarding whether the elements set by structure of organization and some patterns of strategy apply to the corporate governance of Bank in Indonesia. Questionnaires will be distributed according to a specific sampling design. The specific qualitative research method will only be adopted for this study in case of need and a combination of questionnaire and interview will be used in order to get an in-depth understanding of the study area. Moreover, semi-structured interview will be selected as the most appropriate method in the primary data collection, as it was perceived to be cost effective and time saving than face to face interview. In addition to that, face to face interviewing to some big banks will be conducted appropriately.

RESULT AND DISCUSSION

Corporate Governance and Corporate Strategy

Research on strategy of company so far has mainly focus on traditional strategy and its effect on corporate financial performance, and much less attention has been given to how specific strategy and organization structure attributes influence to corporate governance. Shapiro *et al* (2015:61) found that corporate governance and ownership affect innovation activity as company’s strategy more strongly when innovation is measured by patenting activity, rather than new product sales. Corporate governance comes as a set of practices which aims to improve strategic management of the companies, maximizing their value and shareholder return. It has been found a greater valorisation of the company shares with corporate governance practices (Goncalves *et al.*, 2012). On the other hand, Rao and Tilt (2015) critics the existing literature on the relationship between corporate governance, in particular board diversity, and both corporate social responsibility (CSR) and corporate social responsibility reporting (CSRR). Assuming that both CSR and CSRR are outcomes of boards’ decisions (corporate strategy), they propose that examining boards’ decision making processes with regard to CSR would provide more insight into the link between board diversity and CSR.

Board diversity will have more strategy with probability has different pattern and also structure organisation as found by Rose and Bernard (2015) that centralized authority and management provides for optimal decision making in large organizations by using Arrowian framework. Elements within the organization, beyond the central authority, occasionally may have superior information or decision-making skills. Organisational structure also become a subject of research by Gerard and Weber (2015), where they use theoretical analysis of compliance structures and seek to further understanding of corporate governance by examining advantages and disadvantages of positioning the compliance function at various locations within the organisational structure but it does not suggest which structure is more appropriate to improve corporate governance. The pattern of strategy is very unique for further research combining with organisation structure and its effect to corporate governance of Bank in Indonesia.

Pattern of Strategy

Camino and Ayala (2015) disagreement on the definition of strategy by Mintzberg (1988) and Caffé (1985) maintains that almost all definitions are classified into linear, adaptive, and interpretative models that reflect semantic preferences and different perspectives. Their opinion is that the diversity is also due to the divergence between analytical and psycho-social perspectives on strategy.

Van den Steen (2012) defines an explicitly formulated 'strategy' as the 'smallest set of choices and decisions sufficient to guide all other choices and decisions,' which formally captures the idea of strategy as a plan boiled down to its most essential choices. He shows that this definition coincides with the equilibrium outcome of a game where a person can "at a cost" look ahead, investigate, and announce a set of (intended or actual) choices to the rest of the organization. Strategy is also in some precise sense - the smallest set of decisions that needs to be decided centrally to ensure that all decisions are consistent (by giving a clear direction).

In late 2009, Gartner introduced Pattern Based Strategy (PBS) as, "The environment after the recession means business leaders must be more proactive in seeking patterns from conventional and unconventional sources that can positively or negatively impact strategy or operations, and set up a consistent and repeatable response by adjusting business patterns". According to David Jones, CEO of Lanner Group, PBS is an umbrella term that overarches a coalition of existing technologies and suggests how they can be developed. Structurally, PBS is based on four disciplines: (1) the creation of a performance driven culture; (2) the seeking of new patterns; (3) the development of an 'operational tempo'; (4) the use of transparency as a competitive weapon.

Pattern of strategy is commonly used in IT industry, especially in the software programming. For example: a robot application as seen in Figure 1 below.

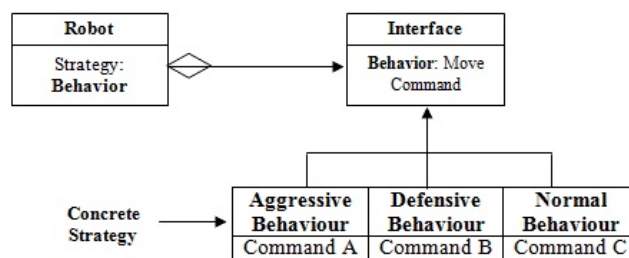


Figure 1 Pattern of Strategy Example in IT Industry

Let's consider an application used to simulate and study robots interaction. For the beginning a simple application is created to simulate an arena where robots are interacting. We have the following classes; (i) Behavior (Strategy) - an interface that defines the behaviour of a robot; (ii) Concrete Strategies: Aggressive Behaviour, Defensive Behaviour, Normal Behaviour; each of them defines a specific behaviour. In order to decide the action this class needs information that is passed from robot sensors like position, close obstacles, etc; (iii) Robot - The robot is the context class. It keeps or gets context information such as position, close obstacles, etc, and passes necessary information to the Strategy class.

For a simple explanation about the pattern of strategy as follows:

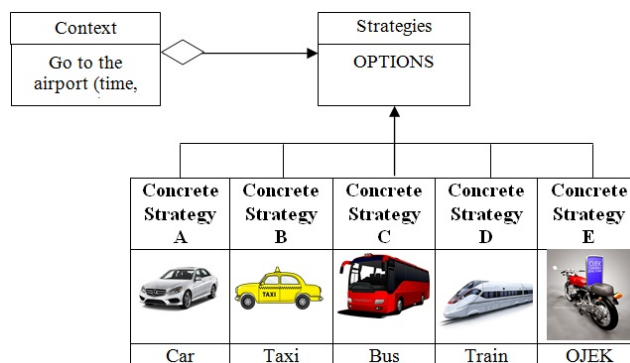


Figure 2. Pattern of Strategy Another Example

From the figure 2, some patterns can be created. For example: Ojek from home to bus station, from bus station to the train station and then continue to the airport by train. This kind of pattern can be implemented in the business with some options to achieve the target of company and the pattern of strategy itself can be different for each company, even each decision maker's behaviour and finally affect to the corporate governance implementation.

A final result on the value of strategy that a pattern of strategy creates more value when the interactions are all complements than when they are (irreducibly) a mixture of complements and substitutes. The reason is that in an environment with all complements, it is very important to get all decisions right, whereas with a mix of substitutes and complements there is always some compromise even in the optimal outcome. This result, which is about the pattern of interactions, suggests some caution on how to interpret the informal finding that successful strategies tend to be very well aligned: such a high degree of alignment is often due not only to skill (developing a great strategy) but also to luck (being in a super modular environment that doesn't force a trade-off in alignment) (Dirlik and Unal, 2014).

Indonesian Board Structure

Corporate governance theory usually concerns the ownership structure of firms, the relationships among shareholders and the firms' management, and, in certain views, the more subtle and diverse relationship existing between the firm and a complex network of stakeholders influencing its behaviour. To deal with such issues, corporate governance theory draws on economics to analyze incentive systems, hierarchical responsibilities, task allocations and managerial control mechanism that aim at aligning the interest of economic actors such as large stockholders, small stockholders, firm management and governmental agencies, so that their behavior will converge.

Indonesian companies adopted the same system with European Continental e.g. dual-board model (two tier board system). Under dual-board model, a company has two boards: the board of directors that has to conduct company's operation, and the commissioners board that has to check the board of directors' results. The board system used in Indonesia is unique. The main characteristics of the system at other countries is: the commissioners board or usually called as supervisory board, was chosen by and should be responsible to General Meeting of Shareholders (GMS), and then they will choose board of directors (Lukviarman, 2004). While in Indonesia, The Law Number 40 of 2007 on Limited Liability Company stated that both are chosen by and be responsible to GMS, as stated as follows : in the

event of the appointment, replacement, or dismissal of members of BOD and/or BOC, BOD must notify the Minister of Law and Human Rights ("Minister of Law") within a period of not more than 30 (thirty) days as from the date of GMS resolution of the change in the members of BOD and/or BOC for the recording in the company registry. This brings a uniqueness on the practice of board governance in Indonesia (Portier, 2012) .

Good Corporate Governance (GCG)

The term of Corporate Governance was barely presented before the decade of 90's, although unclassified and non-scientifically proved evidence exist since the date of Adam Smith. Unfortunately, the usage of Corporate Governance did not follow the rapid research of the concept of Corporate Governance. It can be characterized as a system of principles, which are concerned about the management and the administration of organizations. Through Corporate Governance organizations can be more efficiently governing, transparent, and can control the actions as well as the proceedings of managers (Toudas and Athanasios, 2014).

GCG has been widely acknowledged as the global best standard of corporate governance practices. Indonesian business society has been started to implement the standard since 2001. But many corporations currently still struggle to find their best model on GCG implementation. Wibowo, *et al*, (2015) recommends a strategic model for the implementation of GCG in Indonesia. The model uses a system approach as the analytical basis to connect the implementation of GCG with the strategic context of the company. It includes the utilization of multi-stakeholder, strategic responses, and global benchmarking analysis as the useful tool to guide the strategic implementation of GCG.

Corporate Governance in Indonesian Banking

GCG as stated in Guideline of Good Corporate Governance for Indonesian Banking issued by the National Committee of Corporate Governance Policy on October 17, 2006 consist of five main principles of governance: (1) transparency, (2) accountability, (3) responsibility, (4) independency and (5) fairness. According the research of Doddy and Phua (2013) show that corporate governance practice in Indonesia

is still low. Indonesian firms tend to compensate their poor corporate governance through higher dividend payment. There is a negative effect of corporate governance on dividend payment. Therefore this research confirms the application of substitution theory in Indonesia rather than outcome theory. Subsequent analysis shows that: poor structure and procedures in the board of commissioners, and poor disclosure practices are negatively related to dividend policy, while shareholder rights does not. From the fundamental factor test, growth and firm profitability are positively associated with the dividend policy while firm size is not.

The structure of Corporate Governance in Indonesia is much influenced by various factors, particularly by the continental European system which establishes two-tier system under the concept of insider system with the structure of shareholding concentrated on a few parties (regional government) whereby they exercise their dominant control and influence. The dualistic characteristics (i.e. the functions of providing services and fostering income) of the regional governments results in the less optimum performance of the companies (Kholil, 2015).

Strategy to Improve a Good Corporate Governance

According to Montgomery (2012), strategy was taught as part of the general management curriculum in business schools fifty years ago. In the academy as well as in practice, it was identified as the most important duty of the chief executive officer, the person with overarching responsibility for setting a company's course and seeing the journey through. This vital role encompassed both formulation and implementation: thinking and doing combined.

Mintzberg H and J.A Waters (1985; 948 hal) said that strategy is pattern and called as "intended strategy", because it has not been implemented and orientated to the future or also called as "Realized Strategy" because already been implemented by the organization.

Managers face three central questions in evaluating their company's business prospects: What's the company's present situation? Where does the company need to go from here? How should it get there? Arriving at a probing answer to the question

"What's the company's present situation?" prompts managers to evaluate industry conditions and competitive pressures, the company's current performance and market standing, its resource strengths and capabilities, and its competitive weaknesses.

This definition of strategy comes up with some idea to improve strengths and capabilities of a company and at the end of the day will arrive on how the corporate governance works. In the banking industry, since it has been introduced by Financial Services Authority (formerly known as Bank Indonesia) in 2006, most of the CEO and senior manager just trying to meet conditions set by Financial Services Authority, especially banks under category book 1 and book 2.

In general, they only focus on the fulfilment of the structure and not on the process so that the outcome is not as expected. On the other hand, corporate governance is considered as the cost of compliance, when they implemented the cost will increase and impact to the performance of company is most likely very slim, so that eventually they returned to the traditional business where business is the most important thing and compliance issues carried out in accordance with the requirements only including ignoring the principles of good corporate governance such as transparency, accountability, responsibility, independence and fairness. It is because too focused on the business and the need to continue to grow, then the asset growth strategy and competition becomes more dominant, so that the structure of the organization formed to support more business, while business ethics and compliance issues to be number two.

The corporate governance matter to Investors, because investors need to ensure that their fund invested in a company will give value and secure. It can only be obtained if corporate governance is executed carefully, so a proper strategy and appropriate organizational structure will add value to the company in the eyes of investors. But improved corporate governance is not only an investment issue: it provides a platform for better and more strategic decision-making on environmental and social practices, benefiting society and economies as a whole.

According to Kelly (2004), the patterns presented here consciously lack the implementation guidance commonly included with patterns. This is because these patterns deal with issues of strategy, the implementation of such strategies is varied and complex and therefore outside the scope of these patterns. Further patterns are needed to detail implementation issues.

The framework of study about the pattern can be explained in a simple way as seen in Figure 3 below.

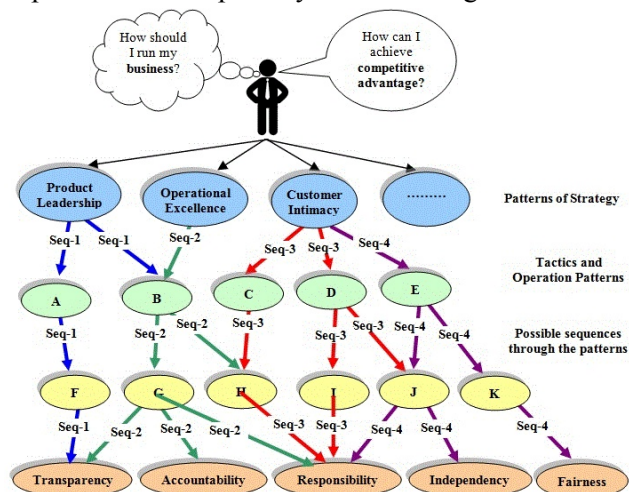


Figure 3. Strategy Pattern Framework

Strategy patterns lead to other patterns; there are many sequences through the pattern language. There are multiple ways to implement each of these strategies, for example, product leadership could be produced through spent relatively high cost for R&D to create an excellent product/service with excellent return, vertically integrated corporation producing every product/service from internal/external resources, alternatively, it could be achieved by a firm with practically no assets at all but sub-contracts and outsourcing agreements with many competitive vendors.

CONCLUSION

Conclusion

Pattern of strategy and organization structure have significant impact to the implementation of good corporate governance in Indonesian Banking, which is not only realized strategy as the main factor but also need to pay attention to the intended strategy as well. Top management has to involve determining appropriate strategy and eliminating unnecessary organization structure, because the long organization

structure would have negative impact to the implementation of good corporate governance partially.

The missing link during this time is actually the combination of appropriate strategy and effective organisation structure (not more than 3 layers) have a significant impact to establish good awareness and understanding about corporate governance in order to improve bank performance, protect stakeholders' interests and increase compliance to prevailing regulations and general code of conduct in the banking industry.

Suggestion

For the next researcher, strongly suggested to include behaviour of top management (risk taking, risk mitigate or risk avoidance) and type of board system as dependent variables, while performance as the independent variable. Regulator and government need to establish a common guideline for good corporate governance implementation considering the type of board system of Indonesia.

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