THE ROLE OF CORPORATE GOVERNANCE MECHANISMS IN ENHANCING PROFITABILITY: AN EMPIRICAL ANALYSIS OF MANUFACTURING COMPANIES

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Abstract – *This study examines the influence of corporate governance mechanisms—specifically the audit committee, independent commissioners, managerial ownership, and institutional ownership—on financial performance, measured by Return on Assets (ROA), in manufacturing companies listed on the Indonesia Stock Exchange during the period from 2019 to 2023. Using a quantitative approach and panel data regression analysis on 117 manufacturing firms, the research aims to provide a deeper understanding of how governance factors contribute to corporate profitability. The results indicate that the audit committee and institutional ownership do not have a significant effect on ROA, as their roles are more preventive and focused on risk management and long-term governance, which do not directly impact asset performance. Managerial ownership also shows no significant effect, primarily due to its relatively small share proportion and the potential entrenchment effect, which reduces incentives to improve performance. Conversely, independent commissioners have a positive and significant impact on ROA, playing a crucial role in strengthening oversight, enhancing accountability, and driving operational efficiency, which directly contribute to increased company profitability. These findings underscore the importance of independent commissioners in the corporate governance of manufacturing companies to support improved financial performance.*

Keywords: *Corporate Governance, Profitability, Corporate Oversight, Operational Efficiency, Manufacturing Sector*

I. INTRODUCTION

The manufacturing sector is a key pillar supporting national economic growth due to its significant contributions to job creation, value-added enhancement, and exports. However, the performance of this sector experienced considerable pressure, particularly during the COVID-19 pandemic, when various production activities were disrupted. One indicator reflecting this condition is the Indonesian Manufacturing Purchasing Managers' Index (PMI), which sharply declined to 27.5 in April 2020—the lowest level in recent years—signaling a severe contraction in national manufacturing activity (Kusumah, 2020). This decline was driven by several factors, including disruptions in the global supply chain, mobility restrictions imposed by lockdown policies, and decreased demand in both domestic and international markets. This phenomenon not only indicated a general slowdown in operations but also significantly impacted the profitability of manufacturing firms, which faced reduced revenues, increased operational costs, and liquidity pressures. Therefore, it is crucial to conduct an in-depth study of the sector's profitability to better understand corporate financial resilience amid external shocks and to formulate more adaptive recovery and growth strategies in the face of economic uncertainty.
Research on the influence of corporate governance mechanisms on financial performance, particularly Return on Assets (ROA), has been extensive but yielded inconsistent results. Several previous studies, such as (Islam, 2024; Oroud, 2019; Rahma et al., 2023; Sofiana et al., 2019), found that the audit committee, independent commissioners, managerial ownership, and institutional ownership significantly affect ROA. These findings suggest that the implementation of sound governance principles can strengthen oversight effectiveness and managerial decision-making, thereby enhancing

corporate profitability. Conversely, studies by (Apriliani et al., 2023; Salehi et al., 2018; Yuliandhari & Novitasari, 2020) concluded that these governance variables do not significantly impact ROA. This inconsistency highlights a critical research gap warranting further investigation. Accordingly, this study aims to re-examine the roles of the audit committee, independent commissioners, managerial ownership, and institutional ownership in influencing ROA, to provide more comprehensive and relevant empirical evidence regarding corporate governance dynamics within the manufacturing sector.

II. LITERATURE REVIEW

This study is grounded in Agency Theory, which highlights the conflict of interest between owners (principals) and managers (agents) arising from the separation of ownership and control within a company. In this context, various corporate governance mechanisms are designed to mitigate potential managerial misconduct that may harm shareholders. For instance, the audit committee and independent commissioners play crucial roles in overseeing management functions, aiming to reduce information asymmetry and prevent opportunistic behavior by management (Simanjuntak & Sinaga, 2021). Furthermore, managerial ownership is regarded as a tool to align the interests of managers and shareholders, as managers with company shares are more incentivized to make decisions that sustainably enhance firm value (Pramudya et al., 2022). On the other hand, institutional ownership serves as an effective external monitor; institutional investors typically possess the capacity, incentives, and influence to pressure management to remain focused on achieving the company's long-term objectives, including profitability improvement (Sakawa & Watanabel, 2020). Therefore, within the framework of Agency Theory, the presence of a strong corporate governance structure involving these four elements can significantly help reduce agency conflicts and ultimately contribute to improved financial performance, particularly in terms of Return on Assets (ROA).

Hypothesis: The Effect of the Audit Committee on Return on Assets

The effectiveness of audit committees plays a vital role in enhancing corporate profitability, particularly as measured by Return on Assets (ROA). According to agency theory, a well-functioning audit committee helps reduce agency costs by closely monitoring financial reporting and managerial decision-making. Empirical evidence supports a significant positive relationship between audit committee characteristics—such as independence, meeting frequency, and expertise—and ROA (Alabdullah & Ahmed, 2020). Similarly, (Shatnawi et al., 2021) report that both the independence and size of audit committees contribute significantly to improved financial performance. Furthermore, (Abraham et al., 2024) emphasize that strong audit committee oversight—especially through the appointment of qualified auditors and rigorous financial reviews—curbs managerial opportunism, enhances transparency, and is positively correlated with higher ROA. Thus, across various contexts, the presence, composition, and activity level of audit committees are closely associated with reduced managerial excesses and more efficient asset utilization, ultimately leading to improved profitability.

Hypothesis: The Effect of Independent Commissioners on Return on Assets

The presence of independent commissioners plays a crucial role in improving Return on Assets (ROA) by minimizing agency conflicts and strengthening corporate oversight functions. As neutral supervisors unaffiliated with management, independent commissioners have the capacity to demand managerial accountability, suppress opportunistic behaviors, and promote more transparent and accurate financial reporting, thereby enhancing corporate profitability (Islam, 2024). Empirical studies indicate that board meeting frequency—which reflects the level of independent oversight engagement—positively correlates with ROA, suggesting that active independent commissioners can reduce operational inefficiencies (Wulandari & Hermanto, 2022). Moreover, increased board independence and size, representing broader external supervision, have been shown to significantly improve financial performance (Islam, 2024). Additionally, independent commissioners with strong professional reputations can enhance reporting quality and accountability, ultimately exerting a positive impact on profitability (Wulandari & Hermanto, 2022). Therefore, the presence of independent commissioners not only increases investor confidence and corporate governance quality but also supports optimal asset utilization through effective and competent oversight.

Hypothesis: The Effect of Managerial Ownership on Return on Assets

Significant managerial ownership is often associated with improved Return on Assets (ROA) because it helps minimize agency conflicts and align the interests of managers and shareholders. Within the framework of Agency Theory, when managers hold a substantial ownership stake in the company, they are more motivated to act in the company's long-term interest, including optimizing asset value, rather than pursuing personal gains. (Sofiana et al., 2019) found that managerial ownership has a positive and significant effect on ROA, supporting the argument that strong internal monitoring can reduce the need for external oversight and promote operational efficiency. Similar findings were reported by (Alabdullah, 2018; Shan, 2019), who assert that increased managerial ownership strengthens the relationship between financial performance and firm value, as managers who are also owners have greater incentives to sustain financial performance improvements. Therefore, managerial ownership serves as an effective internal governance mechanism that not only enhances managerial accountability but also contributes to the optimization of asset utilization and overall corporate profitability.

Hypothesis: The Effect of Institutional Ownership on Return on Assets

Institutional ownership plays a crucial role in influencing Return on Assets (ROA), as institutions, being major shareholders, typically have greater incentives and capacity to exercise rigorous oversight over management policies and actions. Such effective monitoring not only reduces the potential for opportunistic managerial behavior—such as self-serving decision-making—but also fosters operational efficiency through performance monitoring and disciplined strategy implementation. Research by (Abedin et al., 2022) found that an increased proportion of institutional ownership is significantly and positively correlated with ROA, indicating that the presence of institutional investors enhances the efficiency of corporate asset management. This aligns with (Chen, 2025) findings, which conclude that institutions actively involved in corporate governance tend to improve financial performance, including asset profitability. Thus, institutional ownership functions not only as a source of capital but also as a strategic external governance mechanism that ultimately contributes to the sustainable achievement of the company's financial objectives.

III. METHODS

This study aims to provide empirical evidence on the influence of the Audit Committee, Independent Commissioners, Managerial Ownership, and Institutional Ownership on Return on Assets (ROA) in manufacturing companies listed on the Indonesia Stock Exchange from 2019 to 2023. The research employs a quantitative approach using panel data regression analysis to examine the simultaneous relationships among the variables. The population consists of all manufacturing sector companies, totaling 169 firms. Purposive sampling was applied based on the following criteria: (1) companies listed on the Indonesia Stock Exchange during the 2019–2023 period, (2) companies that consistently published financial reports, and (3) companies that use the Indonesian Rupiah as the reporting currency. Based on these criteria, a sample of 117 companies was selected.

Secondary data were utilized, obtained from the companies' annual financial statements during the observation period. The independent variables include audit committee size, proxied by the number of audit committee members; independent commissioners, measured as the ratio of independent commissioners to total commissioners; managerial ownership, measured by the ratio of shares owned by commissioners and directors to the total outstanding shares; and institutional ownership, measured by the ratio of shares owned by institutional shareholders to total outstanding shares. The dependent variable, Return on Assets (ROA), is measured by the ratio of net income after tax to total assets. Data analysis involved descriptive and inferential statistics, including model selection tests (Chow and Hausman tests), classical assumption tests (normality, heteroscedasticity, multicollinearity, and autocorrelation), and hypothesis testing (t-test, F-test, and determination coefficient R^2). This analysis aims to quantitatively and objectively assess the significance and strength of the influence of each independent variable on firm value.

IV. RESULTS AND DISCUSSION

Descriptive Statistics

Descriptive statistics are employed to provide an overview of the research data characteristics, specifically focusing on the minimum, maximum, mean, and standard deviation values for each variable. The results of this descriptive analysis offer preliminary insights into the central tendency and dispersion of the data, as well as assist in identifying potential outliers or high variability within the sample. The following table presents the descriptive statistics of the study:

Table 1. Descriptive Statistics Results

Variable	Mean	Std	min	max
KA	3,000000000	0,3477145032	0,000000	5,000000
KIND	0,416416218	0,1060959586	0,000000	0,833333
KM	0,056628899	0,1230995315	0,000000	0,682759

KINS	0,806098430	0,1816301266	0,133407	0,999985
ROA	0,036938921	0,1257503847	-1,049839	0,943569

The descriptive statistics in this study indicate that Return on Assets (ROA), as the primary indicator of corporate financial performance, has an average value of 3.69%, suggesting that, on average, companies are able to generate profits from their assets, albeit at a relatively moderate scale. However, the distribution of ROA values is quite extreme, with a minimum of -104.98%, a maximum of 94.36%, and a standard deviation of 0.1258. This reflects a high disparity in companies' efficiency in utilizing assets, ranging from those experiencing significant losses to those achieving substantial profits. Meanwhile, the average number of audit committee members (KA) is three, indicating a tendency among companies to form audit committees with a common or standard structure. The relatively low variability, reflected in a standard deviation of 0.3477, shows consistency in audit committee size across most firms. However, the presence of companies with zero audit committee members suggests that some firms have yet to establish or activate an audit committee, potentially affecting the effectiveness of corporate oversight and governance.

Other variables reveal diverse corporate governance structures. The average proportion of independent commissioners (KIND) is 41.64%, with moderate dispersion, indicating variation in board independence levels across companies. Some firms have a high proportion of independent commissioners, while others have few or none at all. Managerial ownership (KM) averages 5.66% but exhibits a relatively high standard deviation of 0.1231, reflecting significant disparity in managerial shareholding—from companies without managerial ownership to those where management holds a dominant stake of nearly 68.28%. In contrast, institutional ownership (KINS) is notably dominant, with an average of 80.61% and a maximum value approaching 100%, demonstrating that institutional investors significantly control the majority of shares in most companies. Nevertheless, the considerable variation across firms suggests that the degree of institutional ownership—and thus institutional influence on management and corporate policies—differs among companies.

Regression Model Testing

The results of the regression model testing in this study indicate that, based on the Chow test with a probability value of 0.0000—well below the significance threshold of 0.05—the fixed effects model is significantly more appropriate than the common effects model. This suggests that there are meaningful differences between individual entities within the sample that must be specifically accounted for. Furthermore, the Hausman test results, with a probability value of 0.045 (also below 0.05), reinforce the choice of the fixed effects model over the random effects model, as they indicate the presence of correlation between the independent variables and individual effects that cannot be ignored. Therefore, based on these two tests, the fixed effects model is selected as the most suitable and reliable model for the data analysis in this study. Consequently, the Lagrange Multiplier test is unnecessary, and the entire analysis focuses on the fixed effects approach as the primary model to produce more accurate and valid estimations.

Classical Assumption Testing

Normality Test

Table 2. Kolmogorov-Smirnov Test Results

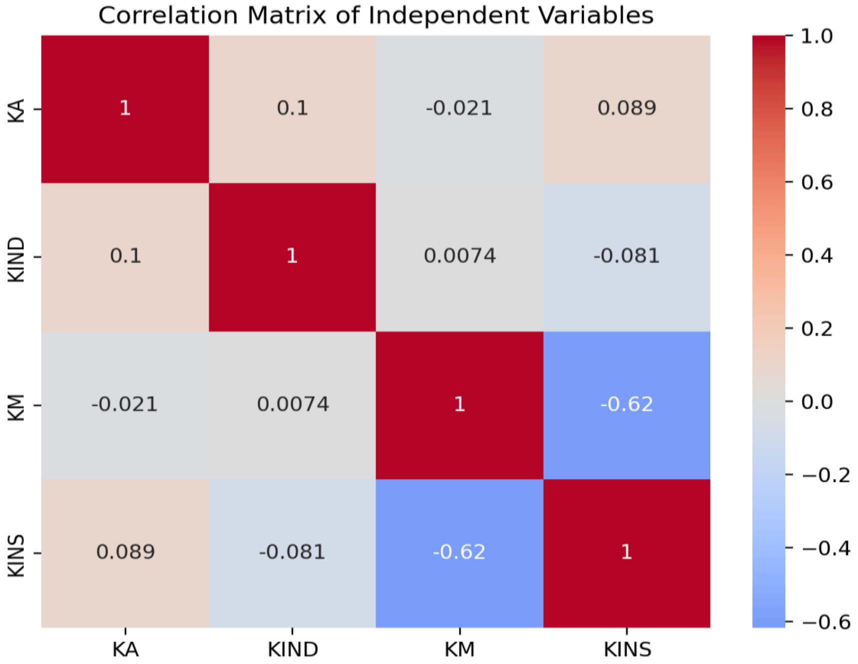
Variable	KS-Statistic	*p-value*	Conclusion
KA	0,0221832824	0.9294532796	There is no heteroscedasticity
KIND	0,017533468	0.9924721525	There is no heteroscedasticity
KM	0,0195345345	0.9757484586	There is no heteroscedasticity
KINS	0,0177007237	0.9915638882	There is no heteroscedasticity
ROA	0,024997394	0.8489449061	There is no heteroscedasticity

Based on the results of the normality test conducted using the Kolmogorov-Smirnov method, all variables used in this study—namely, KA (Audit Committee Size), KIND (Proportion of Independent Commissioners), KM (Managerial Ownership), KINS (Institutional Ownership), and ROA (Return on Assets)—exhibited p-values above the 0.05 significance threshold. This indicates that the distribution of data for each variable follows a normal distribution pattern, suggesting no violation of the normality assumption. In addition, the results also imply the absence of heteroscedasticity, meaning the residuals exhibit constant variance across observations. Therefore, the data's compliance with these classical assumptions provides a solid and valid foundation for proceeding with panel regression analysis, ensuring that the resulting estimations are both reliable and unbiased.

Multicollinearity Test

The results of the multicollinearity test indicate that there is no multicollinearity problem within the regression model. The highest correlation between independent variables was observed between Managerial Ownership and Institutional Ownership, with a value of −0.617. Although this represents a moderate negative relationship, it remains within an acceptable tolerance level and does not indicate an excessively strong linear association. Moreover, most of the other pairwise correlations among independent variables are below 0.75, reflecting generally weak relationships. Therefore, the model is free from multicollinearity issues that could compromise the validity of the regression estimates.

Table 3. Results of the Multicollinearity Test



Heteroscedasticity Test

Table 4. Results of the Heteroscedasticity Test

Variable	Rho	*P-value*
KA	-0.0101080151	0.807259-158
KIND	-0.0651794106	0.1153066254
KM	0.0344522744	0.4055478145
KINS	-0.0210440655	0.6114844521

The results of the heteroscedasticity test indicate that there is no heteroscedasticity problem in the model. This is evidenced by the p-values of the four independent variables (KA, KIND, KM, and KINS), all of which are above the 0.05 significance level and therefore statistically insignificant. Additionally, the Rho coefficients for each variable are relatively small and do not display any specific pattern. These findings suggest that the assumption of homoscedasticity is met, allowing the regression model to be used without the interference of non-constant residual variance.

Autocorrelation Test

Table 5. Results of the Autocorrelation Test

LM Statistic	LM *P-value*	F-Statistic	F-P value

119.913094	5.57E-25	37.12744	1.22E-27

The results of the autocorrelation test show that the F-probability value (p-value) is greater than 0.05. Based on the decision rule, this indicates that the model does not suffer from autocorrelation. This suggests that the residuals are not correlated across time periods, thereby satisfying one of the key assumptions of the regression model.

Panel Data Regression Analysis

Table 5. Results of Panel Data Regression

Variable	Beta	*P-Value*	Conclusion
Const	0,0435979927	0,3553625339	
KA	-0,0072777033	0,5863741506	Not significant
KIND	0,1849498516	0,0000657803	Significant positive effect
KM	0,0379259108	0,2977520103	Not significant
KINS	0,0285016762	0,2543398510	Not significant

Based on the results of the study, it can be concluded that the constant value of 0.043 indicates that when all independent variables are equal to zero, the Return on Assets (ROA) remains at a level of 0.043, reflecting the baseline level of financial performance in the absence of the examined governance factors. Among the independent variables analyzed, the proportion of independent commissioners exhibits the most significant positive effect on ROA, with a regression coefficient of 0.184. This suggests that increasing the proportion of independent commissioners substantially contributes to more effective asset utilization. Managerial ownership and institutional ownership also have positive effects on ROA, albeit to a lesser extent, with regression coefficients of 0.037 and 0.028, respectively. Conversely, the number of audit committee members shows a negative relationship with ROA, with a regression coefficient of -0.007. Although the impact is relatively minor, it may indicate that merely increasing the number of audit committee members does not necessarily enhance asset performance and could, in some cases, be counterproductive.

However, based on partial testing using p-value analysis, only the proportion of independent commissioners (KIND) was found to have a statistically significant effect on Return on Assets (ROA), with a p-value below the 0.05 significance threshold. This finding indicates that an increase in the proportion of independent commissioners can meaningfully enhance a company's financial performance by improving the efficiency of asset utilization. In contrast, other variables—such as the number of audit committee members, managerial ownership, and institutional ownership—did not demonstrate a significant influence on ROA within the context of this study. This suggests that the roles and contributions of these governance and ownership structure variables are less dominant in shaping financial performance. Thus, the findings underscore the relatively more critical role of independent commissioners in influencing the effectiveness of asset management compared to other corporate governance mechanisms.

Discussion: The Effect of the Audit Committee on Return on Assets

Based on the findings of this study, the audit committee does not have a statistically significant effect on Return on Assets (ROA). This suggests that while the presence of an audit committee may enhance the quality of internal oversight, its impact is more preventive in nature and does not directly contribute to improvements in asset utilization efficiency as reflected by ROA. (Abraham et al., 2024) emphasize that the audit committee's role primarily lies in mitigating financial risk and reducing performance volatility, thereby fostering greater managerial and operational stability. However, such stability does not necessarily translate into higher profitability as measured by ROA, given that ROA is influenced by a broader set of factors such as operational strategies, production efficiency, and asset structure. In other words, while the audit committee helps to establish a governance environment conducive to sound financial performance, it does not guarantee immediate or direct improvements in asset returns.

Discussion: The Effect of Independent Commissioners on Return on Assets

The findings of this study indicate that independent commissioners have a significant positive correlation with Return on Assets (ROA), primarily due to their role in enhancing corporate oversight and transparency. As individuals who are not affiliated with the company's management, independent commissioners are able to provide more objective perspectives in strategic decision-making processes. This result aligns with the findings of (Ali et al., 2022; Itan & Angellina, 2023), who demonstrate that the presence of independent commissioners significantly improves firm profitability by strengthening the quality of oversight and promoting more accountable corporate governance. By reducing potential conflicts of interest and reinforcing managerial supervision, independent commissioners contribute to greater operational efficiency, which is ultimately reflected in higher ROA. These findings reinforce the argument that the presence of independent commissioners—unencumbered by managerial ties—supports management efficiency, enhances accountability, and improves the return on corporate assets.

Discussion: The Influence of Managerial Ownership on Return on Assets

The results of this study indicate that managerial ownership does not have a significant effect on Return on Assets (ROA). A primary reason for this finding is the relatively low proportion of shares owned by management, which averaged only 5% in this study. Such a modest ownership stake is insufficient to strongly motivate management to enhance the efficiency of asset utilization within the firm. Additionally, low managerial ownership tends to fail in optimally aligning the interests of management with those of shareholders, thereby providing little incentive for improving financial performance (Cheng et al., 2023). Managerial ownership may also induce an entrenchment effect, whereby managers feel overly secure in their positions, leading to reduced incentives to innovate or improve operational efficiency (Waseem et al., 2023). These findings suggest that without complementary incentive mechanisms and adequate oversight, managerial ownership alone is unlikely to be effective in driving improvements in corporate asset performance.

Discussion: The Influence of Institutional Ownership on Return on Assets

Based on the findings of this study, institutional ownership does not exhibit a significant effect on Return on Assets (ROA). This outcome may be attributed to several factors, one of which is that although institutions generally possess greater resources and supervisory capacity compared to individual shareholders, their influence over daily operational decisions and asset utilization efficiency is often limited (Cao et al., 2020; Moradi et al., 2022). Furthermore, institutional investors tend to focus more on long-term risk management and corporate stability, prioritizing governance and transparency aspects rather than directly enhancing operational performance that impacts ROA (Huang et al., 2023). Therefore, while the presence of institutional investors can strengthen oversight mechanisms, their impact on the company's asset profitability is not always immediate or significant.

V. CONCLUSION

The results of this study indicate that the audit committee and institutional ownership do not have a significant effect on Return on Assets (ROA). Although the audit committee can enhance the quality of internal supervision and help reduce risks and performance volatility, its impact is more preventive and does not directly improve asset utilization efficiency or overall profitability. Similarly, despite institutional ownership possessing greater resources and supervisory capacity, its influence on operational decisions and asset efficiency tends to be limited, as institutional investors primarily focus on long-term risk management and corporate governance.

On the other hand, managerial ownership also does not significantly affect ROA, largely due to the relatively small proportion of shares owned by management, which limits their ability to align interests with shareholders and drive operational efficiency. Additionally, low managerial ownership may lead to an entrenchment effect, where management feels secure in their position, thereby reducing motivation to innovate and improve performance. In contrast, the presence of independent commissioners shows a positive and significant correlation with ROA, owing to their objective role in supervision and strategic decision-making, which enhances operational efficiency and company profitability through improved governance quality and accountability.

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