CHAPTER II
LITERATURE REVIEW

2.1 Introduction

Literature review is an excellent way to synthesizing research findings to show evidence on a meta-level and to uncover areas in which more research needed,which is a critical component of creating theoretical frameworks and building conceptual models (Snyder, 2019). In this chapter provides the previous studies, theory that used in this research, research framework and hypothesis.

2.2 Theory of the Study

2.2.1 Agency Theory

Agency theory discusses the relationship between two entities, namely principal and agent. According to Jensen and Meckling (1976), there are two types of agency relationships: managers and shareholders and managers and lenders (bondholders). contract between the manager (agent) and the investor (principal). Agency conflicts that occur in companies are not only between shareholders and managers but also between shareholders who control management and small shareholders who cannot effectively control management. Through the financial reports which are the responsibility of the agent, the principal can measure, assess and at the same time monitor the agent's performance to what extent the agent has acted to maximize the welfare of the principal.

Jens and Ruback (1983) argue that the most expensive agency problem is shown in the results of financial reports published by managers who do not meet standards. The concept of corporate governance, which is based on agency theory, is expected to function as a tool to provide confidence to investors that they will receive a return on the funds they have invested by selecting a qualified auditor. Corporate governance is closely related to how to make investors believe that managers will benefit them, believe that managers will not steal or take advantage of them, and that managers will not steal or take advantage of other people. This theory has a relationship between the director and the company's financial performance

2.3 Financial Performance

The company was founded with the aim of improving financial performance to increase the prosperity and wealth of the owners. If a company performs well, it has a good effect (repson) for stakeholders. With its wealth, the company can improve the welfare of its stakeholders (Muchtar & Darari, 2017). Financial performance can provide an overview of the work performance and financial condition of a company over a certain period. Company profits can show their financial performance. The more profit that is made, the better the financial performance achieved. It shows the company's ability to manage existing resources, which makes it important.

The leadership of the board of directors is responsible for the success of the company in the long term (Wijayanti & Mutmainah, 2012). This organization is responsible for setting company policies and strategies. If companies want to survive in the long run, they must control resources, according to resource dependence theory (Pfeffer & Salinsik, 1978). Available resources are essential for business growth and sustainability.

To bring valuable resources to the company, the board of directors builds external relationships with existing connections and networks. Because of this, racial diversity on the board of directors is critical to Improving financial performance through innovation and decision making. performance improvement can occur with the large number of members of the board of directors through their role in formulating policies within the company. Directors do not only focus on one thing if the number is relatively large. Directors can also be deployed to areas under their control and make them more focused on the tasks and authority given.

2.4 Board Size

According to Sukandar and Rahardja (2014) found that more members of the board of directors can improve performance because of their role in formulating company policy. If there are many things, directors don't concentrate on one. Research results on board size are inconsistent. Yasser et al. (2017), Martín & Herrero (2018), and Daromes & Jao (2020) found that the financial performance of companies is better with a larger number of boards of directors. The joining of new members increases the knowledge of the firm, increasing profitability. In contrast, Liang et al. (2013) found that when the number of boards of directors increases, causes a decrease in financial performance. According to Wijayanti and Mumtamainah (2012) and Asengga et al. (2018), the size of the board of directors does not affect business performance.

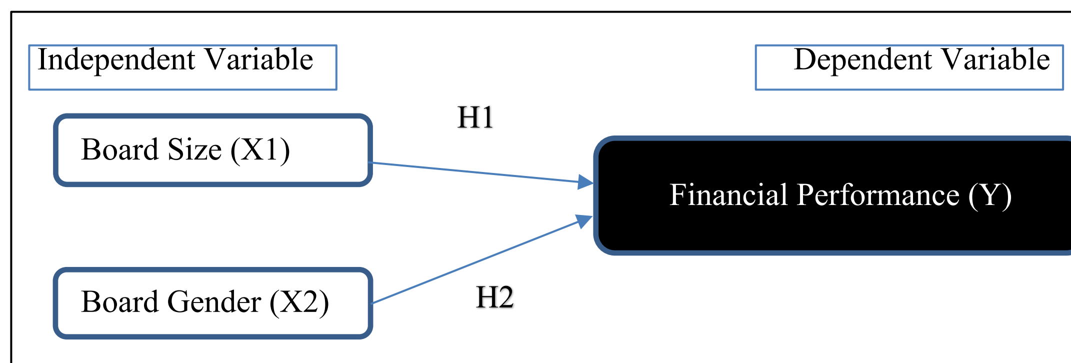
2.5 Board Gender

According to Kusumastuti, (2007), Women are considered more deserving of holding important positions in companies, the presence of women in top management in Indonesia is still under-recognized. In addition, there is an opinion that men's success in leadership is caused by ability and women's success is caused by luck. According to Gary and Gneezy (2004), women invest less than men. This is because women are more aware of risks compared to men, which results in a lower proportion of women in several positions compared to men. However, Darmadi's research findings (2011) show that women's involvement in the board of directors affects business performance. Compared to men, women on the board of directors know more about company finances.

Most people believe that women leaders have innovation and the ability to make better decisions, which have a positive impact on company performance. Studies conducted by Alvarez and McCaffery (2000), Carter et al. (2007), and Kusumastuti (2007) found that the gender differences indicated by the spread of boards affect firm performance. believes that the decisions made can increase the value of the company if the structure of the board of directors is more diverse (Rose, 2007)

2.6 Conceptual Framework

Figure 2.1 Conceptual Framework Between Independent Variable and Dependent Variable



In this study there are two independent variables and one dependent variable. Independent variables divided into two which are board size and board gender. Dependent variable in this study is financial performance.

2.7 Research Hypothesis

Based on the theory used and previous studies, this sub-chapter will explain the hypotheses formulated in this study. For this purpose, hypotheses were developed based on the conceptual framework identified in the previous section.

2.7.1 Composition Board Size on Company Financial Performance

The size of the board of directors has a significantly positive effect on a company's financial performance. The results of Sam'ani (2008) show that the size of the board of directors is positively related to company performance, and good company performance will follow by better financial performance. This research is supported by the research by Ridho and Aditya (2013), which shows that there is a significant positive effect between board size and company performance. The board of directors has a very important role in a company because they are different from the board of commissioners and have great authority to manage company resources. The board of directors is responsible for determining the direction of the company's resource policies and strategies, both short and long term.

According to Study by Hardikasari (2011) states that many studies have shown that companies with large boards cannot communicate, coordinate, and make better decisions than companies with smaller boards. However, Dalton et al. (in Hardikasari, 2011) found that there is a positive correlation between large board sizes and companies with smaller boards. From the description above, the hypothesis can be formulated as follows:

H1: *The size of the board of directors has a positive effect on financial performance manufacture company listed in Indonesia exchange (IDX).*

2.7.2 Composition Gender Board of Directors on Company Financial Performance

There are differences between a male manager and a female manager in terms of emotional stability, aggressiveness, leadership ability, self-confidence, and openness. The female board of directors has an inclination to do analysis, where the strategy they determine is believed to have been based on careful consideration and is able to deliver performance in a better direction, so that in the end it encourages the provision of intellectual capital information (Rasmini, Wirakusuma, & Yuniasih, 2014). Some research found that the proportion of women on the Board of Directors significantly affects the company's financial performance (Dewi, 2016), (Fathonah, 2018). According to directors (Luckerath-Rovers, 2013) and (Low et al., 2015) women on the board of directors the presence of women on the board of directors can increase firm value and reduce the level of company risk if female directors are led rather than male directors. Thus the first hypothesis is proposed as follows:

H2*: The proportion of women on the Board of Directors has a positive effect on financial performance manufacture company listed in Indonesia exchange (IDX).*

2.8 Summary

The factors that influence financial performance, theories that related on board characteristic to financial performance and also the gaps that resulted from previous studies. Furthermore, this chapter also presents the research framework for this study and the development of the study's hypotheses.

Literature review is an excellent way to synthesizing research findings to show evidence on a meta-level and to uncover areas in which more research needed,which

is a critical component of creating theoretical frameworks and building conceptual models (Snyder, 2019). In this chapter provides the previous studies, theory that used in this research, research framework and hypothesis.