

CAN PSAK 71 INCREASE FINANCIAL STABILITY DURING THE COVID 19 PANDEMIC? (SURVEY ON CONVENTIONAL BANKS IN INDONESIA IN 2020)

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ABSTRACT

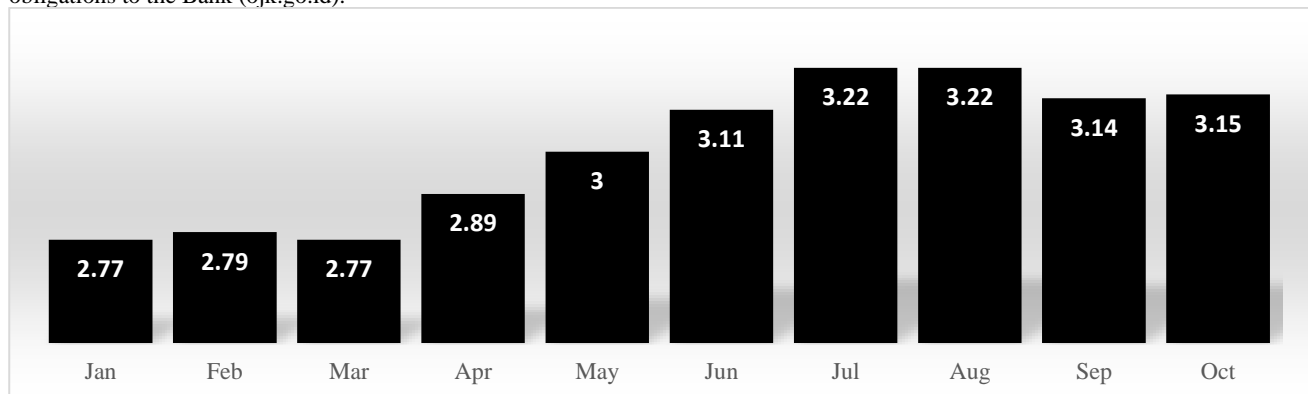
The object of this research is PSAK 71 (IFRS 9) as the independent variable and Financial Stability as the dependent variable. This study aims to test whether PSAK 71 (IFRS 9) can increase the financial stability of the banking sector during the Covid-19 pandemic. The research method used is a causal study. The population in this study were all conventional banks in Indonesia. The sampling technique used is purposive sampling. The sample in this study is conventional banks listed on the IDX in 2020. The data collection technique used is by using secondary data in the form of conventional commercial bank annual reports, Indonesian Banking Statistics data, and macroeconomic data needed in the calculations. Statistical analysis used is simple linear regression analysis. The test results show that PSAK 71 has a positive effect on financial stability. That means the higher application of PSAK 71 can increase financial stability of conventional banks in Indonesia.

Keywords: expected credit loss, financial stability, PSAK 71

INTRODUCTION

In early December 2019, the whole world was shocked by the emergence of cases Covid-19 virus. This case first appeared in the city of Wuhan, China, then spread and infects almost all countries in the world, including Indonesia. The Covid-19 pandemic have a negative impact on the global economy. The International Monetary Fund (IMF) noted that the global economy has fallen into a crisis, after around 95% of countries in the world are projected to experience contraction. In addition, the Covid-19 pandemic has also caused global economic losses of US \$12 trillion (Warta Ekonomi.co.id).

In Indonesia, economic conditions in the first quarter of 2020 grew by 2.97% from the fourth quarter of 2019. Then, in the second quarter there was a growth contraction of -5.32%. Furthermore, in the third quarter, economic conditions again grew by 5.05% (bps.go.id). If you pay attention, the growth contraction in the second quarter occurred when Covid-19 first entered Indonesia. With the Covid-19 pandemic, in addition to affecting the pace of the economy, it also has an impact on the company's business activities, such as the banking sector, one of which is lending. Credit that is disbursed by banks to customers is not necessarily all collectible. This is referred to as credit risk, namely the risk due to the failure of the debtor and/or other parties to fulfill their obligations to the Bank (ojk.go.id).



Picture 1
NPL Development of Commercial Banks in Indonesia in 2020

Based on Figure 1, it can be seen that from March since the Covid-19 case entered Indonesia until October the Non Performing Loan (NPL) ratio continued to increase. NPL is a ratio to measure how big the number of non-performing loans is. The greater NPL ratio, the greater number of non-performing loans. If this is allowed, it can disrupt the financial stability of banks. The Otoritas Jasa Keuangan (OJK) stated that the risk that often accompanies financial stability is credit risk.

Financial stability is a condition in which the financial system consisting of financial institutions, financial markets and financial infrastructure is able to withstand stress so that the financial intermediation process is not disrupted (Gadanec & Jayaram, 2008). Financial instability can be triggered by various causes and fluctuations, and can be sourced from external (international) and internal (domestic). The risks that most often accompany activities in the financial system include credit risk, liquidity risk, market risk, and operational risk (Ministry of Finance). The main risk that often occurs in the implementation of bank credit is credit risk, namely the risk that arises when the debtor fails to fulfill the obligation to pay the principal or interest installments as agreed in the credit agreement. Financial instability in the banking sector has a negative impact, namely the loss of public confidence in the intermediation function of financial institutions, a decline in economic growth, and the cost of recovery due to the crisis has increased.

On April 15, 2020, OJK has issued guidelines for accounting treatment related to the application of PSAK 71 (IFRS 9) regarding Financial Instruments. This PSAK 71 replaces PSAK 55 and has been effective since January 1, 2020. The most basic difference between PSAK 71 and PSAK 55 is related to the calculation of Allowance for Impairment Losses, which is a reserve prepared by banks to face the risk of impairment losses on asset, such as a loan or credit. This PSAK 71 fundamentally changes the method of calculation and reserve of provision losses due to bad loans (tirto.id).

In PSAK 55, Allowance for Impairment Losses is calculated using the incurred loss method which is backward-looking, where Allowance for Impairment Losses is formed when an event that causes the risk of default has occurred or when there is objective evidence that the debtor is experiencing impairment, such as late paying credit installments. Meanwhile, if PSAK 71, Allowance for Impairment Losses is calculated using the forward-looking expected loss method, where Allowance for Impairment Losses is formed apart from past data, also from the estimated risk of financial instruments since the beginning of the credit period and applies to all credit categories, such as current loan, doubtful loan and non-performing loan. Forward-looking information that is usually used is the projection of economic growth, inflation, unemployment rate, and the commodity price index at each reporting date. Realizing that the Covid-19 pandemic has a significant impact, the banking sector is expected to be able to implement PSAK 71 in order to consider whether a financial asset, in this case a loan, has an increased risk or not, and then the company can determine how much reserves must be set aside, so that banking financial stability can be maintained.

Based on the background described previously, here the author wants to find out how the effect application of PSAK 71 on banking financial stability during the Covid-19 pandemic. Therefore, here the author will take the title "**Can PSAK 71 (IFRS 9) Increase Financial Stability during The Covid-19 Pandemic?**".

LITERATURE REVIEW

Stewardship theory was first discovered by Lex Donaldson and James H. Davis in 1991. This theory describes a situation where managers are not motivated by individual goals, but rather aimed at their main goals for the benefit of the organization. This theory has a psychological and sociological basis that has been designed, where executives as stewards are motivated to act according to the wishes of the principal. In addition, steward behavior will not leave the organization because the steward tries to achieve the goals of the organization. This theory is designed for researchers to examine situations, where executives in the company as stewards can be motivated to act in the best way on their principals.

The allowance for impairment model, in this case the allowance for credit losses, in IAS 39 only recognizes losses that occur at the balance sheet date, so an allowance for losses is provided if there is objective evidence as a result of past events. However, the financial crisis has drawn attention to the discrepancy between loss events and their recognition (Schmidt, et. al. (2015); Gebhardt (2016); Hashim, et. al. (2016)). Moreover, its "backward-looking" nature has the potential to exacerbate the crisis situation (Marton and Runesson, 2017). Allowance for credit losses under IAS 39 is rated "too little and too late" (Hoogervorst, 2014). The risks inherent in assets are not properly reflected (ESRB, 2017). In response to this criticism, IASB urged to revise accounting standards related to Financial Instruments and issued IFRS 9.

In the IFRS 9 allowance method, the IASB introduces a model that looks at future conditions, namely the Expected Credit Loss (ECL) model. This change can counter the weakness of loss recognition in IAS 39. As a consequence, the requirement to determine allowance for losses in IAS 39 has been removed (Gebhardt (2016) ; Novotny-Farkas (2016)). In IFRS 9, allowance for losses is made at the time the loan is initially extended to the customer. ECL is defined as the probability weighted estimate of credit losses (ie the present value of cash shortfalls). ECL estimates must consider all relevant information, including historical data, current conditions, future forecasts and macroeconomic conditions. Thus, IFRS 9 can significantly expand the information required to determine credit losses.

PSAK 71 was first implemented in Indonesia since January 1, 2020. This PSAK 71 adopted from IFRS 9 replacing PSAK 55 (IAS 39) which discusses Financial Instruments. The most basic difference between PSAK 71 and PSAK 55 is related to the calculation of Allowance for Impairment Losses, which is a reserve prepared by banks to face the risk of impairment losses on assets, such as loans. In PSAK 55, Allowance for Impairment Losses is calculated using the incurred loss method which is backward-looking, where Allowance for Impairment Losses is formed when an event that causes the risk of default has occurred or when there is objective evidence that the debtor is experiencing impairment, such as late paying credit installments. Meanwhile, if PSAK 71, Allowance for Impairment Losses is calculated using the forward-looking expected loss method, where Allowance for Impairment Losses is formed apart from past data, also from the estimated risk of financial instruments since the beginning of the credit period and applies to all credit categories, such as current loan, doubtful loan and non-performing loan. Forward-looking information that is usually used is the projection of economic growth, inflation, unemployment rate, and the commodity price index at each reporting date.

Financial stability is a condition in which the financial system consisting of financial institutions, financial markets and financial infrastructure is able to withstand stress so that the financial intermediation process is not disrupted (Gadanec & Jayaram, 2008). Financial instability can be triggered by various causes and fluctuations, and can be sourced from external (international) and internal (domestic). The risks that most often accompany activities in the financial system include credit risk, liquidity risk, market risk, and operational risk (Ministry of Finance). The main risk that often occurs in the implementation of bank credit is credit risk, namely the risk that arises when the debtor fails to fulfill the obligation to pay the principal or interest installments as agreed in the credit agreement. Financial instability in the banking sector has a negative impact, namely the loss of public confidence in the

intermediation function of financial institutions, a decline in economic growth, and the cost of recovery due to the crisis has increased.

RESEARCH METHODS

The purpose of this study is a causal study, namely a study to test whether one variable causes another variable to change or not. In this study, the researcher is interested in explaining one or more factors that cause the problem. In other words, the aim of the researcher to conduct a causal study is to be able to state that the X variable causes the Y variable (Sekaran and Bougie, 2017).

The population in this study were all conventional commercial banks in Indonesia, amounting to 96 companies. The sampling method uses purposive sampling, which is a technique that involves selecting subjects who are placed most advantageously or in the best position to provide the required information. This technique is used when the number or category of samples that have limited information and the selection of sample members is based on certain criteria set by the researcher.

The sample criteria are as follows:

- a. Conventional commercial banks that publish annual reports for 2020.
- b. Conventional commercial banks that publish the ratio of Allowance for Impairment Losses to Productive Assets.

The sample is part of the number and characteristics possessed by the population. The sample of this study is conventional commercial banks, totaling 77 companies. The data used in this study are secondary data taken from the 2020 annual reports of conventional commercial banks, Indonesian Banking Statistics data, and other macro information. This secondary data is data that has been processed by the company and has been published in the form of an annual report, or in other words, the data is not directly taken from the company concerned but is obtained from the website of each company.

The independent variable in this study is PSAK 71 which is measured using the Expected Credit Loss (ECL) model from PSAK 71 with the formula:

$$ECL = \text{Probability of Default (PD)} \times \text{Loss Given Default (LGD)} \times \text{Exposure At Default (EAD)}$$

Information :

- ECL = Allowance for credit losses
 PD = Probability of customers failing to pay credit
 LGD = Losses that will be suffered by the bank
 EAD = Outstanding credit declared in default

After that, the ratio of Allowance for Impairment Losses to Productive Assets is calculated with the formula:

$$\text{Allowance for Impairment Losses Ratio} = \frac{\text{Allowance for Impairment Losses}}{\text{Productive Asset}} \times 100\%$$

The dependent variable in this study is Financial Stability which will be measured using the Financial Stress Index (FSI) approach. The first step taken to form the FSI is to find the weight of each variable. The weight of each variable is obtained from the regression results with the following model:

$$FAIL_t = \beta_0 + \beta_1 CMAX_t + \beta_2 IS_t + \beta_3 RS_t + \beta_4$$

Information :

- FAIL_t = Number of failed banks with NPL ratio criteria 5% in period t
 CMAX_t = Stress on rupiah exchange rate against US\$ in period t
 IS_t = Idiosyncratic stress in period t
 RS_t = Risks spread in period t
 NPL_t = Non-performing loan in period t

After obtaining the coefficients for each variable, the coefficients are used as weights in the FSI calculation. The FSI calculation based on Illing and Liu (2003) is as follows:

$$I_t = \sum_{i=1}^k \omega_i \frac{X_{i,t} - \bar{X}_i}{\sigma_i}$$

Information :

- I = Financial Stress Index value in period t
 X = Value of variable i in period t
 \bar{X} = The average value of the variable i
 σ = Standard deviation of variable i
 ω = Variable weight i

RESULTS AND DISCUSSION

In this section, researchers will describe the results of research related to the effect of the application of PSAK 71 on financial stability in conventional commercial banks in Indonesia in 2020.

a. Correlation Analysis and Coefficient of Determination

Table 3 Coefficient of Determination Analysis

Model Summary ^b				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
	.463 ^a	.214	.204	1187.90547
a. Predictors: (Constant), ECL				
b. Dependent Variable: FAIL				

Based on Table 3, it can be seen that the value of the correlation coefficient obtained by the PSAK 71 (X1) variable with the financial stability variable (Y) is 0.463. The correlation value is positive which indicates that the relationship between the independent variable and the dependent variable is unidirectional, where the better PSAK 71, the more financial stability will be followed. Based on the correlation coefficient interpretation criteria, the correlation value of 0.463 is included in the category of moderate relationship, which is in the interval 0.60-0.799.

Based on Table 3, information is obtained that the R-square is 0.214 or 21.4%. This value indicates that the PSAK 71 variable contributes or influences the financial stability variable by 21.4%. While the remaining 78.6% is influenced by other variables not examined.

b. Simple Linear Regression Analysis

Table 4 Simple Linear Regression Analysis

Coefficients ^a						
Model	Unstandardized Coefficients			Standardized Coefficients	t	Sig.
	B	Std. Error	Beta			
(Constant)	12722.499	631.251		20.154	.000	
ECL	.219	.048	-.463	4.521	.000	
a. Dependent Variable: FAIL						

Based on Table 4, the following equation is obtained:

$$Y = 12.722 + 0,219X1$$

From the results of a simple linear regression equation can be interpreted as follows:

- a. The constant of 12.722 states that if PSAK 71 is worth 0 (zero) and there is no change, then financial stability will be worth 12.722 units.
- b. The value of the X1 variable, namely PSAK 71, has a regression coefficient of 0,219, meaning that if PSAK 71 increases by one unit, financial stability will increase by 0,219 units.

Hypothesis Designing:

H₀ : β₁ = 0, PSAK 71 has no effect on Financial Stability

H_a : β₁ ≠ 0, PSAK 71 has an effect on Financial Stability

Information :

- With a significance level of 0,05
- Criteria : Reject H₀ if t count > t table, accept in other cases

Based on Table 4, it can be seen that the t count value obtained by the PSAK 71 (X1) variable is 4,521. This value will be compared with the t table value in the t distribution table. With = 0,05, df = n – k – 1 = 77 – 1 – 1 = 75, the t table value for the two-party test is 1,992. From the values above, it can be seen that the t count value obtained by the PSAK 71 (X1) variable is 4,521 > t table (1,992), in accordance with the hypothesis testing criteria that H₀ is rejected and H_a is accepted. This means partially, PSAK 71 has a positive effect on financial stability (Y).

c. Discussion

The test results show that PSAK 71 has a positive effect on financial stability. This means that the higher the application of PSAK 71, the higher the financial stability of conventional commercial banks in Indonesia. The results of this study support the research of Mushkudiani, Z. (2016) which states that the Expected Credit Loss model in IFRS 9 includes a set of relevant information to expect credit losses in the future. This model makes allowance for losses carried out at the beginning and the amount of the allowance will be greater so that it will limit the possibility of high distribution of dividends and bonuses. With this provision, it will reduce the accumulation of losses during the "boom" period, so that reducing concerns about the lack of capital adequacy. IFRS 9 can mitigate the provision of procyclical credit losses and improve financial stability.

The results of research by Novotny-Farkas, Z. (2016) stated that the allowance for losses in IFRS 9 was carried out earlier, the amount of the allowance was larger and in line with regulations. Provision is made at the beginning to reduce the accumulation of losses. So, it can be concluded that IFRS 9 can improve financial stability. The results of the research by Sanchez Serrano, A. (2018) stated that the allowance for expected credit losses turned out to produce more timely and complete information to bring great benefits to financial stability. The results of the research of Kund, A. G. and Rugilo, D. (2019) stated that IFRS 9 has succeeded in reducing the level of "cliff-effect", this goal is achieved because the allowance for losses uses the Expected Credit Loss model. This has a positive effect on financial stability and bank resilience. The research results of Kund, A. G. and Rugilo, D. (2020) state that the cliff-effect of IAS 39 has decreased since the enactment of IFRS 9, where the model used in IFRS 9 can improve financial stability of the banking sector in the future.

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