

# **Partial privatization and its effect on structure, conduct, performance in the Indonesian commercial banking market**

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**A thesis submitted for the degree of Doctor of Philosophy in Economics**

**of**

**the University of Canberra**

**August 2013**

## Abstract

This study aims to evaluate the link between partial privatization of state-owned banks and the impact on the performance of firms and also to examine the relationship between partial privatization of state-owned banks and the impact on market structure. In order to examine the effect of partial privatization of state-owned banks on market structure, conduct and performance, this study divides the time frame into three phases: the deregulation phase, the restructuring and partial privatization phase, and the divestment phase. Initially, the study examines the effect of partial privatization of state-owned banks on market structure and indirectly on firms' behaviour using the Panzar and Rosse model. Then the study separately evaluates the impact of the partial privatization on firms' performance using the performance variables. The results from the Indonesian banking market structure show that the commercial banking market is found to be highly competitive during 1997 to 2003 or in period 2, yet, the  $H$  statistics from 1992 to 2011 were in the area of monopolistic competition. The results from the performance of Indonesian state-owned banks post partial privatization during 2004 to 2011 or in period 3 suggest that merged banks significantly improved profitability and economic efficiency and also decreased credit risk exposure. Overall state-owned banks performances after partially privatized in the short term, however, decreased economic efficiency. In the long run, the performance of state-owned bank improved profitability and efficiency.

**Keywords:** partial privatization, state-owned banks, market structure, firm conduct, firm performance, market of competition, Industrial organization theory, Panzar and Rosse model, performance variables, quantitative approach.

## **Dedication**

This thesis is dedicated to my father, Bapak Soekotjo. My memories of your support, love, affection, and faith will always live on.

## **Acknowledgement**

All the praise be to Allah SWT, who has given me opportunity, strength and ability to complete this milestone and made my wishes come true.

For his support, guidance, mentoring, encouragement and faith, I would like to thank my primary supervisor, Associate Professor Cameron Gordon. Thank you so much for sharing your thoughts, knowledge, and experiences during my study and thesis writing process. I also would like to thank Dr Chris Sadleir, my secondary supervisor, for his ideas and coaching.

My deepest gratitude goes to the Indonesian Higher Education General Directorate (DIKTI) for the scholarship to pursue a doctoral degree at the University of Canberra. A particular thank you is given to the Department of Business Administration, Faculty of Administrative Science, University of Brawijaya, where I work as a lecturer. For giving an opportunity to me to have further study in overseas. I would like to thank mbak Ima and mbak Parti, Bank Indonesia staffs, who spent their effort and time to provide a specific data that is mostly needed in this study.

Appreciation also extended to my colleagues in the faculty, particularly those who supported a lot through good and bad time. I would like to thank Wike, Firda Hidayati, Yeney Prihatiningtias, Kunta Nugraha, Melyanti and Fiona Buick. I would like also to thank Diane Philips, for giving me an opportunity to work as a tutor in the faculty. Hope our friendship will last forever.

Family contributes the greatest part of my PhD journey. I would like to express my deepest gratitude and appreciation for the support and encouragement of my family. For their love, support and patience, I would like to thank my husband (Heri Prayitno), my mum (Nuke Soekotjo), and my three lovely kids: Adela, Ferdy and Dimas. I am truly thankful for their amazing support, encouragement, tears and laughs together you always extended to me.

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## Abbreviation

ADB	: Asian Development Banks
AFR	: Average Funding Rate
ATM	: Automated Teller Machine
Bank EXIM	: Bank Export Import
BBD	: Bank Bumi Daya
BCA	: Bank Central Asia
BDN	: Bank Dagang Negara
BDMN	: Bank Danamon
BII	: Bank International Indonesia
BNI	: Bank Negara Indonesia
BAPINDO	: Bank Pembangunan Indonesia
BRI	: Bank Rakyat Indonesia
BSF	: Bank-Specific exogenous Factors
BTN	: Bank Tabungan Negara
CAMEL	: Capital, Asset, Management, Earning, and Liquidity
CAR	: Capital Adequacy Ratio
CD	: Certificate of Deposit
CR	: Concentration Ratio
DM	: Deposit Mix
EH	: Efficiency Hypothesis
EU	: European United
FSDP	: Financial Sector Development Project
GDP	: Gross Domestic Product
HI	: Herfindahl Index
IBRA	: Indonesian Banking Restructuring Agency

IBS	: Indonesian Banking Statistics
IDX	: Indonesian Stock Exchange
IMF	: International Monetary Fund
IR	: Interest Revenue
JCI	: Jakarta Composite Index
MSME	: Micro, Small, and Medium Enterprises
NIM	: Net Interest Margin
OECD	: Organization for Economic Cooperation and Development
OI	: Other Income
PCE	: Price of Capital Expenditure
PNB	: Private National Bank
PPE	: Price of Personnel Expenses
P-R	: Panzar and Rosse
REPELITA	: The Government five-year economic plan
ROE	: Return on Equity
SBCSC	: State Bank Credit Supervision Committee
SCP	: Structure-Conduct-Performance
SOB	: State-Owned Bank
SOE	: State-Owned Enterprise

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