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The Influence Of Financial Health On Bank Financial Performance

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ABSTRACT
This study aims to analyze the impact of bank financial health on financial performance using a quantitative method and multiple regression analysis. The research population consists of banks listed on the Indonesia Stock Exchange (IDX), while the sample is selected using the purposive sampling method, based on the availability of complete financial data. The independent variables used in this study are Capital Adequacy Ratio (CAR), Loan to Deposit Ratio (LDR), Non-Performing Loan (NPL), Operating Expenses to Operating Income (BOPO), and Net Interest Margin (NIM), with Return on Equity (ROE) as the dependent variable. The results indicate that NIM has a significant positive effect on ROE, while BOPO has a significant negative effect. Meanwhile, CAR, NPL, and LDR do not have a significant impact, suggesting that capital adequacy and credit risk are more related to long-term stability rather than profitability. The regression model explains 30.3% of ROE variability, with the remainder influenced by external factors. These findings emphasize that operational efficiency and optimal net interest margin management are crucial in improving bank profitability.

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INTRODUCTION

Banking plays a crucial role in a country's economy as an intermediary institution that collects and distributes public funds. The stability of the banking sector heavily depends on the financial health of the bank itself, which reflects its ability to manage risks and generate optimal profitability (Wulansari & Chandra, 2022). Therefore, it is essential to understand how factors influencing the financial health of banks can impact their financial performance.

The financial health of banks is typically assessed using specific methods, such as the Risk-Based Bank Rating (RBBR) and CAMEL (Capital, Asset, Management, Earnings, and Liquidity). These bank health indicators are commonly used to evaluate the sustainability of bank operations and profitability (Dewi & Yadnyana, 2019). Some of the common ratios used to assess a bank's financial health include the Capital Adequacy Ratio (CAR), Loan to Deposit Ratio (LDR), Non-Performing Loan (NPL), and Operating Expenses to Operating Income (BOPO) (Fiola, 2024).

In this context, research shows that bank health variables significantly affect financial performance. For example, a high CAR ratio can increase investor confidence, but if not accompanied by operational efficiency, it can hinder profitability (Susilowati & Siregar, 2022).

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On the other hand, a high Non-Performing Loan (NPL) level can indicate significant credit risk, which can negatively impact the bank's Return on Assets (ROA) (Fakhruddin & Purwanti, 2015).

According to research conducted by Astutik & Djazuli (2014), the Loan to Deposit Ratio (LDR) is an important indicator in assessing a bank's health. The higher the LDR, the greater the bank's credit distribution, but if too high, it can increase liquidity risk. Other studies also show that a high BOPO ratio indicates low operational efficiency, which can hinder a bank's profitability growth (Utami & Utami, 2021).

The bank health assessment system in Indonesia has evolved from the CAMEL method to RGEC (Risk Profile, Good Corporate Governance, Earnings, and Capital), which places greater emphasis on risk aspects and corporate governance (Hanantijo, Armayasari, & Respati, 2018). In this system, Good Corporate Governance (GCG) becomes a key factor determining a bank's credibility and resilience in facing economic pressures (Irawati, Maksum, Sadalia, & Muda, 2019). Additionally, a bank's profitability is also influenced by the management of operational costs and tax strategies. Some studies show that tax avoidance practices, within certain limits, can enhance the profitability of Islamic banks by reducing tax burdens, but if not properly controlled, they can pose legal and reputational risks (Susilowati & Siregar, 2022). Furthermore, research conducted by Komara (2017) suggests that the Capital Adequacy Ratio (CAR) does not always have a significant effect on Return on Assets (ROA) but plays a more crucial role in maintaining long-term capital stability. Conversely, factors such as Net Interest Margin (NIM) and operational efficiency have a more direct impact on bank profitability (Wulansari & Chandra, 2022).

Other empirical studies have found that Islamic banks tend to have lower ROA levels compared to conventional banks, mainly due to higher operational cost structures and the limited availability of financial instruments for investment (Dewi & Yadnyana, 2019). However, with increasing public awareness of Islamic finance, Islamic banks have opportunities to improve their performance through product innovation and operational efficiency (Fakhruddin & Purwanti, 2015). Besides internal factors, macroeconomic conditions also affect a bank's financial health. For example, economic slowdowns and rising interest rates can increase the risk of credit defaults, ultimately impacting NPL ratios and bank profitability (Hanantijo, Armayasari, & Respati, 2018). Therefore, banks need to implement stricter risk management strategies to maintain financial stability amid uncertain economic conditions.

Although numerous studies have explored the relationship between financial health and bank performance, there are still research gaps that need further exploration. Previous studies have focused more on conventional banks (Wulansari & Chandra, 2022), while research on Islamic banks remains limited (Astutik & Djazuli, 2014). Moreover, while some studies have analyzed the impact of NPL, LDR, and BOPO on financial performance, few have examined how these factors work simultaneously within more complex analytical models (Irawati et al., 2019).

Previous studies have also reported mixed results regarding the effect of CAR on ROA, with some studies finding a significant influence (Fakhruddin & Purwanti, 2015), while others found no significant impact (Komara, 2017). This indicates inconsistencies in research

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findings that require further examination, particularly considering moderating or mediating factors such as risk management and macroeconomic conditions. Additionally, research on the impact of Good Corporate Governance (GCG) on bank financial performance still needs deeper investigation, especially in the context of Indonesia's banking sector, which has unique regulations and ownership structures (Dewi & Yadnyana, 2019). Therefore, this study aims to bridge these gaps by further analyzing the relationship between financial health and financial performance in both conventional and Islamic banking sectors.

This research is highly urgent because banking is a sector that significantly influences national economic stability. With increasing global economic challenges, banks must maintain their health to remain competitive and sustainable. Rising NPL levels and low operational efficiency can threaten bank profitability, ultimately affecting national financial stability (Hanantijo, Armayasari, & Respati, 2018). Moreover, the development of financial technology (fintech) and banking digitalization also demands that banks become more adaptive in enhancing operational efficiency (Fiola, 2024). Therefore, a deeper understanding of the factors influencing bank financial health is crucial in determining future banking strategies and policies. Thus, this research not only contributes to academic literature but also provides practical implications for regulators, bank managers, and investors in making better strategic decisions.

METHODS

This study employs a quantitative approach using multiple regression analysis to examine the impact of financial health on bank financial performance. This approach is chosen because it provides objective and measurable results in understanding the relationship between research variables. The data used in this study comes from the financial statements of banks listed on the Indonesia Stock Exchange (IDX). Thus, this research relies on secondary data obtained from official and reliable sources.

The population in this study includes all banks listed on the IDX over a specific period. However, not all banks in the population can be used as research samples. Therefore, the sample is selected using the purposive sampling method based on predetermined criteria, such as banks that have complete financial statements and have not been delisted during the study period. By applying these criteria, the research findings are expected to be more relevant and accurate in depicting the banking sector in Indonesia.

The variables used in this study consist of independent and dependent variables. Bank financial health is the independent variable, measured using several key indicators: Capital Adequacy Ratio (CAR), Loan to Deposit Ratio (LDR), Non-Performing Loan (NPL), Operating Expenses to Operating Income (BOPO), and Net Interest Margin (NIM). Meanwhile, the dependent variable used to measure bank financial performance is Return on Equity (ROE). ROE is chosen as a financial performance indicator because it reflects a bank's effectiveness in managing capital to generate profits for shareholders.

The data analysis technique in this study begins with descriptive statistical analysis to understand the characteristics of the data, such as mean, standard deviation, minimum, and maximum values for each variable. Then, classical assumption tests are conducted, including normality, heteroscedasticity, multicollinearity, and autocorrelation tests. The normality test

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ensures that the data follows a normal distribution, while the heteroscedasticity test detects whether there is an unequal variance of residuals in the regression model. Additionally, the multicollinearity test examines whether there is a high linear correlation between independent variables, and the autocorrelation test identifies whether there is correlation among residuals in the regression model.

Once the classical assumption tests are met, the analysis proceeds with multiple regression analysis to determine the effect of independent variables on the dependent variable. The regression model used in this study is as follows:

$$ROE=\beta0 + \beta1CAR + \beta2LDR + \beta3NPL + \beta4BOPO + \beta5NIM + e$$

In this model, the regression coefficients of each variable will be analyzed to determine the extent to which CAR, LDR, NPL, BOPO, and NIM contribute to changes in ROE. A significance test is also conducted to examine whether independent variables have a significant effect on the dependent variable, both simultaneously through an F-test and individually through a t-test. The results of these tests will serve as the foundation for drawing conclusions regarding the relationship between financial health and bank financial performance.

The interpretation of research findings is based on several key indicators, including regression coefficients, significance levels (p-value), Adjusted R-Square, and Durbin-Watson values. The regression coefficient indicates the direction and magnitude of the effect of independent variables on ROE, while the p-value determines whether the effect is statistically significant. The Adjusted R-Square value illustrates how much variation in ROE can be explained by the independent variables, whereas the Durbin-Watson value is used to detect autocorrelation in the model.

Although this study adopts a systematic approach, several limitations need to be acknowledged. One major limitation is the use of secondary data, which depends on the quality and transparency of financial reports published by banks. Additionally, this study does not incorporate external factors such as macroeconomic conditions and banking regulations, which may also influence bank financial performance. Therefore, the findings should be interpreted while considering these limitations.

The results of this study are expected to provide significant contributions to various stakeholders, particularly regulators, bank management, and investors. For regulators, the findings can serve as a basis for formulating policies aimed at improving the stability of the banking sector. Meanwhile, for bank management, this study helps identify key factors that should be considered to enhance profitability and operational efficiency. On the other hand, investors can use the findings as a reference for evaluating bank performance before making investment decisions.

Beyond its practical implications, this study also opens avenues for future research. Future studies may develop the research model by incorporating additional variables that influence financial performance, such as macroeconomic factors, risk management quality, or corporate governance aspects (Good Corporate Governance). By adopting a more comprehensive approach, future research is expected to provide deeper insights into the dynamics of financial health and bank performance in Indonesia.

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RESULTS AND DISCUSSION

Descriptive Statistics

Table 1. Descriptive Statistics of Bank Financial Health

Statistics		CAR	NPL	NIM	BOPO	Loan To Deposit Ratio
N	Valid	287	287	287	287	287
	Missing	0	0	0	0	0
Mean		26.0314	.6809018	1.7798597	89.7192	84.3412
Median		23.3100	.0300000	.0646000	88.8700	84.2400
Mode		24.00[a]	.00000	.00050	60.58[a]	69.28[a]
Std. Deviation		11.41747	1.14757327	2.31103144	24.54543	23.46678
Minimum		10.52	.00000	-2.58000	18.06	12.35
Maximum		83.35	4.96000	10.45000	261.10	171.32
Sum		7471.00	195.41880	510.81974	25749.41	24205.94

a. Multiple modes exist. The smallest value is shown

The results of the descriptive statistical analysis of bank financial health indicators show significant variations across several fundamental aspects. The Capital Adequacy Ratio (CAR) has an average value of 26.03 with a standard deviation of 11.41. This figure reflects differences in capital adequacy among banks, where some banks have relatively low capital levels with a minimum value of 10.52, while others have significantly higher capital levels, reaching a maximum of 83.35. The median value of 23.31 indicates that half of the banks studied have a capital adequacy ratio below this figure.

Meanwhile, the Non-Performing Loan (NPL) ratio has an average value of 0.68 with a standard deviation of 1.15, indicating differences in credit risk levels across banks. The minimum value of 0.00 suggests that some banks do not have any non-performing loans, while the maximum value of 4.96 indicates that certain banks have a significantly higher level of non-performing loans compared to the industry average. With a median of 0.03, it can be observed that most banks maintain relatively low NPL levels, demonstrating sound credit risk management in the banking sector.

In terms of the Net Interest Margin (NIM), the average value of 1.78 with a standard deviation of 2.31 reflects significant variations in banks' ability to generate net interest income. A minimum value of -2.58 suggests that some banks experience negative interest margins, which may result from high interest expenses or low net interest income. Conversely, some banks have exceptionally high NIMs, reaching 10.45. With a median of only 0.064, it can be concluded that the majority of banks have lower interest margins than the average, possibly due to conservative interest rate policies or intense competition within the banking industry.

A significant variation is also observed in the Operating Expenses to Operating Income (BOPO) ratio, which has an average value of 89.72 and a standard deviation of 24.54. This

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indicates substantial differences in operational efficiency among banks. Some banks demonstrate exceptional efficiency, with BOPO values as low as 18.06, while others struggle with high operating expenses relative to their income, with a maximum value reaching 261.10. With a median of 88.87, most banks exhibit efficiency levels that revolve around this figure.

Meanwhile, the Loan to Deposit Ratio (LDR) presents an average value of 84.34 with a standard deviation of 23.46, highlighting considerable differences in lending policies among banks. Some banks adopt a highly conservative approach in loan disbursement, with a minimum LDR of 12.35, while others are more aggressive in distributing third-party funds, with a maximum LDR reaching 171.32. The median value of 84.24 suggests that the LDR distribution is relatively balanced around the average, reflecting a moderate loan disbursement strategy in the banking industry.

Table 2. Descriptive Statistics of Financial Performance

Statistics		
ROE		
N	Valid	287
	Missing	0
Mean		1.48695609
Median		.11400000
Mode		.010000
Std. Deviation		11.282488061
Minimum		-95.440000
Maximum		27.310000
Sum		426.756397

The descriptive statistical analysis of Return on Equity (ROE) shows significant variations in financial performance among the sampled banks. The mean ROE is 1.49, indicating that, on average, banks generate a relatively low return on equity. However, the standard deviation of 11.28 suggests substantial variability in profitability across different banks. The median ROE is 0.114, which is significantly lower than the mean, indicating that more than half of the banks have an ROE below the average, suggesting the presence of some outliers with extremely high returns. The minimum ROE of -95.44 reveals that certain banks have suffered severe financial losses, while the maximum ROE of 27.31 indicates that some banks have performed exceptionally well. The mode of 0.01 suggests that the most frequently observed ROE value is very close to zero, reinforcing the observation that a significant portion of banks operate with low profitability. The total ROE sum of 426.76 reflects the combined equity return of all banks in the sample.

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Classical Assumption Test

Normality Test

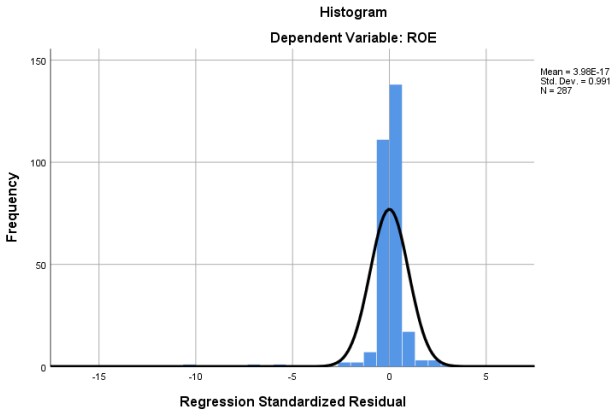

Figure 1. Normality Test

The histogram in Figure 1 shows the distribution of regression standardized residuals for ROE, illustrating an approximately normal pattern. The presence of a bell-shaped curve indicates that the residuals are symmetrically distributed around the mean. Although the overall distribution aligns with the assumption of normality, slight deviations at the tails suggest the possibility of minor skewness or the presence of outliers.

Linearity Test

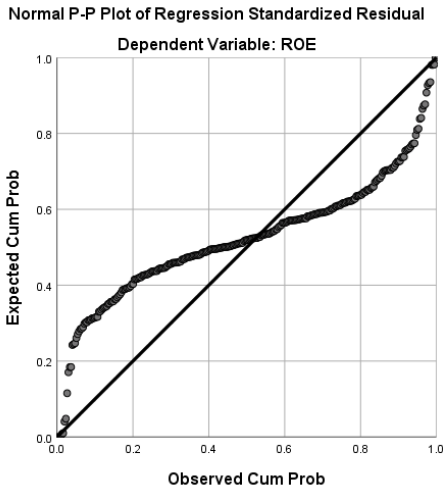

Figure 2. Linearity Test

The P-P Plot in Figure 2 illustrates the relationship between the observed cumulative probability and the expected cumulative probability of the regression standardized residuals for ROE. The data points largely follow the diagonal reference line, suggesting that the assumption of linearity is reasonably met.

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Heteroscedasticity Test

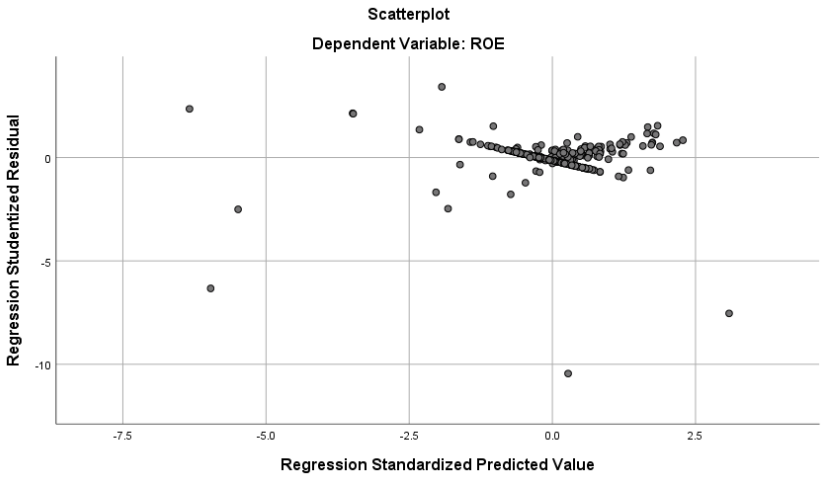

Figure 3. Heteroscedasticity Test

The scatterplot in Figure 3 illustrates the distribution of regression standardized residuals against the standardized predicted values for ROE. The pattern of data points appears somewhat dispersed but shows a tendency to cluster, particularly in certain regions. Ideally, if the assumption of homoscedasticity is met, the points should be randomly scattered without forming a clear pattern.

Multiple Linear Regression

Table 3. Multiple Linear Regression Test

Coefficients[a]

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.	Collinearity Statistics	
		B	Std. Error	Beta			Tolerance	VIF
1	(Constant)	23.326	3.325		7.016	.000		
	CAR	.000	.050	.000	-.003	.997	.951	1.051
	NPL	.495	.584	.050	.847	.397	.704	1.421
	NIM	.779	.288	.160	2.705	.007	.712	1.404
	BOPO	-.237	.023	-.515	-10.163	.000	.965	1.036
	Loan To Deposit Ratio	-.027	.024	-.057	-1.128	.260	.974	1.027

a. Dependent Variable: ROE

The results of the multiple linear regression analysis in Table 3 provide insights into the impact of various financial health indicators on Return on Equity (ROE). The regression model shows that the constant (intercept) has a significant positive value, indicating that when all independent variables are held constant, banks still have a positive baseline ROE. Among the independent variables, Net Interest Margin (NIM) and Operating Expenses to Operating

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Income (BOPO) show statistically significant effects on ROE. The positive coefficient for NIM (B = 0.779, p = 0.007) suggests that higher net interest margins contribute positively to bank profitability. Conversely, BOPO (B = -0.237, p = 0.000) has a strong negative impact on ROE, indicating that banks with higher operating expenses relative to income tend to experience lower financial performance. Meanwhile, Capital Adequacy Ratio (CAR), Non-Performing Loan (NPL), and Loan to Deposit Ratio (LDR) do not show statistically significant relationships with ROE, as indicated by their high p-values (CAR = 0.997, NPL = 0.397, LDR = 0.260). This suggests that capital adequacy and liquidity ratios may not directly influence profitability in the observed period, possibly due to other moderating factors such as risk management strategies and macroeconomic conditions. The Variance Inflation Factor (VIF) values for all independent variables remain below 2, indicating the absence of multicollinearity and confirming that the regression model is stable.

In terms of hypothesis testing, the study supports the hypothesis that NIM has a significant positive effect on ROE (H3 accepted) and that BOPO negatively affects ROE (H4 accepted). However, the hypotheses that CAR (H1), NPL (H2), and LDR (H5) significantly impact ROE are rejected, as their effects are not statistically significant. These findings suggest that while profitability is primarily driven by interest margin and cost efficiency, capital structure and credit risk indicators may not be the most influential factors in determining bank profitability within the given sample.

Table 4. F Test

ANOVA[a]

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	11029.815	5	2205.963	24.427	.000[b]
	Residual	25376.422	281	90.308		
	Total	36406.238	286			

a. Dependent Variable: ROE
b. Predictors: (Constant), Loan To Deposit Ratio, NPL, BOPO, CAR, NIM

The ANOVA F-test results in Table 4 indicate that the regression model is statistically significant in explaining variations in Return on Equity (ROE). The F-value of 24.427 with a p-value of 0.000 suggests that the combination of independent variables (Loan to Deposit Ratio, NPL, BOPO, CAR, and NIM) significantly influences ROE at a 1% significance level. This means that at least one of the predictor variables has a significant impact on ROE, justifying the use of the regression model.

Table 5. Coefficient of Determination

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.550[a]	.303	.291	9.503028621	1.668

a. Predictors: (Constant), Loan To Deposit Ratio, NPL, BOPO, CAR, NIM
b. Dependent Variable: ROE

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The Model Summary in Table 5 shows that the R Square value is 0.303, indicating that 30.3% of the variation in Return on Equity (ROE) can be explained by the independent variables (Loan to Deposit Ratio, NPL, BOPO, CAR, and NIM). The remaining 69.7% is influenced by other factors not included in this model. The Adjusted R Square of 0.291 suggests a slight adjustment for the number of predictors, confirming that the model retains explanatory power.

Discussion

This study reveals that bank financial health has a significant impact on financial performance, with various indicators reflecting different levels of efficiency and profitability among banks. Based on descriptive statistical analysis, there are substantial variations in the Capital Adequacy Ratio (CAR), Loan to Deposit Ratio (LDR), Non-Performing Loan (NPL), Operating Expenses to Operating Income (BOPO), and Net Interest Margin (NIM). This indicates that each bank has a different level of financial health in managing capital, credit risk, operational efficiency, and net interest margin.

In this study, CAR has a relatively high average value, indicating that most banks have adequate capital to mitigate risks. However, in regression testing, CAR does not have a significant effect on ROE, suggesting that a high capital level does not necessarily contribute directly to profitability. These findings align with previous research, which states that CAR plays a more crucial role in maintaining long-term capital stability rather than directly influencing short-term profitability.

Meanwhile, NPL has a relatively low average, indicating that most banks are effectively managing credit risk. However, in the regression analysis, NPL also does not have a significant effect on ROE. This suggests that while non-performing loans can be a burden for banks, their impact on profitability may have been minimized through effective risk mitigation strategies or adequate loss reserves.

The factors that have the most significant impact on financial performance are Net Interest Margin (NIM) and BOPO. NIM has a significant positive effect on ROE, indicating that the higher the net interest margin earned by the bank, the greater the profits generated. This is reasonable since NIM reflects the bank's efficiency in managing interest income relative to interest expenses. Banks with high NIM tend to have better strategies for setting lending and deposit interest rates.

Conversely, BOPO has a significant negative effect on ROE, suggesting that operational efficiency plays a crucial role in determining a bank's profitability. The higher the BOPO, the greater the operating expenses relative to operating income, reducing the bank's net profit. These findings emphasize that controlling operating costs is a key factor in improving financial performance. Therefore, banks that can enhance their operational efficiency will be better positioned to generate higher profits.

The F-test results in ANOVA analysis conclude that, simultaneously, the independent variables used in this study (CAR, LDR, NPL, BOPO, and NIM) have a significant impact on ROE, with a very low significance level. This suggests that although some variables do not have a significant partial effect, the overall combination of financial health factors still contributes to a bank’s performance.

Furthermore, based on the results of the coefficient of determination (R Square), it is found that the independent variables in this model can explain approximately 30.3% of the variability in ROE, while the remaining 69.7% is influenced by other factors not included in this study. This indicates that while financial health factors contribute to financial performance, other external factors such as macroeconomic conditions, regulations, and industry competition may also affect bank profitability.

The findings of this study provide important insights into the key factors affecting bank financial performance. Operational efficiency, as reflected in BOPO, and the ability to generate net interest margin, as reflected in NIM, are the most dominant factors in increasing bank profitability. Meanwhile, capital adequacy ratios and credit risk do not show a significant effect on ROE, suggesting that capital structure and non-performing loans are more related to long-term stability rather than short-term profitability.

Considering these findings, this study recommends that banks focus more on strategies to improve operational efficiency and optimize net interest margin management. Additionally, future research could expand the model by incorporating external factors such as interest rates, inflation, and banking regulatory policies, which may further contribute to the overall financial performance of banks.

CONCLUSION

The results of this study indicate that bank financial health influences financial performance, with Net Interest Margin (NIM) and Operating Expenses to Operating Income (BOPO) being the most significant factors. NIM has a positive impact on Return on Equity (ROE), indicating that banks with higher net interest margins tend to be more profitable. Conversely, BOPO negatively affects ROE, highlighting that operational efficiency is a key factor in improving bank profitability. Meanwhile, Capital Adequacy Ratio (CAR), Non-Performing Loan (NPL), and Loan to Deposit Ratio (LDR) do not show a significant effect on ROE, suggesting that capital stability and credit risk are more related to long-term sustainability rather than direct profitability. The regression model explains 30.3% of the variation in ROE, while the remaining portion is influenced by external factors such as macroeconomic conditions, regulations, and industry competition. Therefore, banks must enhance operational efficiency and net interest margin management strategies to improve their financial performance.

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