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The Influence of Good Corporate Governance Mechanisms, Gender Diversity, and Profitability on Financial Distress

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ABSTRACT

This study examines the influence of Good Corporate Governance (GCG) mechanisms, gender diversity, and profitability on financial distress in manufacturing companies within the consumer non-cyclicals sector listed on the Indonesia Stock Exchange (IDX) from 2018 to 2022. Financial distress is a critical condition that can jeopardize a company's operational continuity. The research method utilized is probit regression analysis, with a sample of 51 companies, resulting in 255 data observations. The findings reveal that institutional ownership and audit committees do not significantly affect financial distress. Conversely, gender diversity has a negative impact, suggesting that diverse perspectives in decision-making processes play a crucial role. Additionally, net profit margin is found to negatively influence financial distress, indicating that companies with lower profit margins are more susceptible to financial challenges. The resulting regression model demonstrates a significant explanatory power for variations in interest coverage ratios based on the examined independent variables. This research provides valuable insights for companies and stakeholders in implementing effective governance practices and considering gender diversity as a factor in financial risk management. The findings are expected to contribute to the advancement of theory and practice in accounting and financial management, while also assisting companies in mitigating financial distress and enhancing long-term performance.

INTRODUCTION

In the business world, companies encounter various challenges that can threaten their operational continuity and financial sustainability. One significant issue is financial distress, which refers to a situation in which a company faces severe financial difficulties, jeopardizing its ability to meet both its financial and operational obligations. If left unaddressed, this can lead to bankruptcy. Financial health is crucial for any company, as it forms the foundation for survival and performance improvement (Stepani & Nugroho, 2020). The manufacturing industry, particularly the consumer non-cyclicals sector, has experienced a decline due to mobility restrictions and disruptions in economic activities. Although this sector is generally regarded as stable and less susceptible to economic cycles, many companies within it still face financial distress. The decline in stock performance mirrors a reduction in income and profits, which in turn heightens the risk of financial distress, especially amid a slowdown in economic activity (Utami et al., 2020). As a result, manufacturing firms have seen a decrease in production activities, leading to lower income and profits (Thalia et al., 2021).

According to Khayati et al. (2022), the consumer non-cyclicals sector is less vulnerable to economic downturns, as it deals with essential goods consumed daily by the public, offering a positive outlook for the sector. This view is supported by Utami (2020), who argues that the consumer sector is resilient and capable of weathering economic crises. While its growth may be slower compared to industries more sensitive to economic fluctuations, the consumer non-cyclicals sector can generate consistent and reliable long-term profits. In 2019, the sector experienced a 16.8% decline in performance, followed by an 11.9% decrease in 2020. This downward trend continued in 2021, when the Indonesia Stock Exchange reported an additional 11.29% drop, ending the year at a value of 16.06%. This decline was attributed to substantial drops in the stock prices of key companies in the sector, with UNVR experiencing a 30.95% decrease and HSMP seeing a 23.26% decline. However, in 2022, stock performance within the manufacturing companies in the consumer non-cyclicals sector improved by 7.9%. Declining stock performance often reflects a downturn in operational performance, which can result in reduced profits. A decline in profits reduces a company's ability to meet interest obligations, thereby increasing the risk of financial distress. In this regard, the Interest Coverage Ratio (ICR) serves as a critical indicator for assessing a company's capacity to cover interest expenses using operational profits (Suranta et al., 2023).

Based on financial reports published on the Indonesia Stock Exchange, PT Tri Bayan Tirta (ALTO) reported negative earnings for five consecutive years, from 2018 to 2022, leading to the closure of its factory in Sukabumi, West Java. Additionally, PT Duta Intidaya Tbk (DAYA) recorded negative earnings for three years, from 2020 to 2022. Meanwhile, PT Daya Putra Utama Makmur (DPUM) filed for a Suspension of Debt Payment Obligations (PKPU) with the Commercial Court in Semarang in September 2022. A lower ICR ratio indicates a heavier debt burden, leaving less capital available for other needs and reducing the ability to meet interest expenses. Previous studies have identified various factors influencing financial difficulties in manufacturing companies within the consumer non-cyclicals sector. Research by Abugri (2022) suggests that good corporate governance can mitigate financial distress, as poor resource management and ineffective governance often contribute to financial difficulties. Other studies indicate that audit committees may play a role in influencing financial distress (Kamau et al., 2023), while some have found that gender diversity negatively impacts financial distress (Lee & Thong, 2023). Conversely, some research suggests that higher profitability ratios may be associated with increased financial distress risks (Dirman, 2020). If not adequately addressed, financial distress can lead to bankruptcy, impacting all stakeholders involved. Consequently, it is essential for companies to identify the factors that contribute to financial distress risk. Business activities always involve various processes of making accurate, careful, and swift decisions, considering that business activities are highly dynamic in relation to prospects and risks (Utami, 2023). This study aims to explore the underlying causes of financial distress, the indicators that can help identify it, and the effects on company performance. Accordingly, the following research questions are formulated:

a. Does institutional ownership have an impact on financial distress?
b. Does the audit committee influence financial distress?
c. Does gender diversity affect financial distress?
d. Does the profitability ratio have an effect on financial distress?

This study aims to identify the factors influencing financial distress, focusing on good corporate governance, gender diversity, and profitability, while also formulating the research problem. The research provides valuable insights and references for stakeholders, academics, and practitioners with an interest in financial issues, supporting decision-making and guiding future research. The study covers the period from 2018 to 2022 within the consumer non-cyclicals manufacturing sector.

LITERATURE REVIEW

Agency Theory

Agency theory explains the relationship between principals and agents, where the agent, as the representative of the company's owners, is responsible for managing operations and reporting performance to the shareholders. Variables such as Good Corporate Governance (GCG), gender diversity, profitability, and financial distress are highly relevant within this framework. GCG plays a vital role in mitigating agency problems by ensuring that management acts in the best interests of the owners. By adhering to the principles of good governance, companies can reduce conflicts of interest and enhance transparency, which, in turn, supports improved company performance. Gender diversity on the board of directors is another crucial factor in this context.

Financial Distress

Financial distress represents a financial risk that can arise during business operations (Mahaningrum & Merkusiwati, 2020). It is essential for managers to implement appropriate plans and policies to prevent such issues, as minimizing financial distress is crucial. Financial distress refers to a situation in which a business faces significant financial difficulties, putting the company at risk of bankruptcy (Tri Arizka et al., 2021). Companies experiencing financial distress often struggle to remain competitive, leading to increased costs and reduced profits. According to Suranta et al. (2023), financial distress is closely related to a company's financial health, as reflected in the Interest Coverage Ratio (ICR). The ICR assesses a company's ability to meet its interest obligations by comparing earnings before interest and taxes (EBIT) with interest expenses. When the ICR is low, particularly below 1, it indicates that the company is not generating sufficient profit to cover its interest payments, thereby increasing the likelihood of financial distress. In other words, an ICR below 1 signals financial distress, while an ICR above 1 suggests a financially healthy company. A declining ICR further heightens the risk of bankruptcy. Additionally, companies that report negative earnings for two consecutive years are typically in a state of financial distress.

Good Corporate Governance

Good Corporate Governance (GCG) is a system that governs and manages companies based on principles of transparency, accountability, and responsibility. The core principles of GCG include transparency, accountability, responsibility, independence, and fairness, all of which play a vital role in ensuring the long-term sustainability and reputation of the company (Tricker, 2021). Moreover, according to Herbert & Agwor (2021), good corporate governance refers to the institutional framework, procedures, and standards that guide and ensure effective organizational management for all stakeholders. GCG is intended to address agency problems that may arise between owners and management (Mappanyukki et al., 2024).

a. Institutional Ownership

Institutional ownership refers to the shareholding held by financial institutions, such as pension funds, insurance companies, and investment managers. It is considered one of the mechanisms of good corporate governance that can mitigate agency problems between owners and managers, thereby aligning the interests of the company's owners and its management. A higher proportion of institutional ownership is associated with more efficient use of company assets, which helps reduce the potential for financial distress (Dirman, 2020).

Research conducted by Patriandari et al. (2023) and Widhiadnyana & Dwi Ratnadi (2019) suggests that institutional ownership has a negative effect on financial distress. Based on this finding, the hypothesis can be formulated as follows:

H1: Institutional ownership negatively impacts the probability of financial distress.

b. Audit Committee

The Audit Committee is a group established by the board of directors to oversee the financial reporting process, internal and external audits, and ensure compliance with relevant regulations. This committee acts as an intermediary between management, auditors, and shareholders, with the objective of ensuring transparency and accountability in the company's financial reporting (Keay, 2023). Furthermore, other studies suggest that the creation of an audit committee within the framework of good corporate governance is intended to oversee the financial statements prepared and disclosed by the company's management (Setiany et al., 2018). Investors provide a high assessment of the quality of financial statements produced by companies that have characteristics of the board of commissioners and audit committee following regulations (Utami et al., 2021).

The competence of the audit committee is a critical factor influencing the company's overall condition. In addition to financial performance, the effectiveness of the audit committee can be used as an indicator of potential financial difficulties. A less effective audit committee may lead to a decline in company performance, thereby increasing the likelihood of financial distress. Research by Saputri (2019) highlights that the effectiveness of the audit committee is crucial for overseeing managerial performance and developing policies related to financial utilization, allowing the company to maintain good financial health as reflected in its financial ratios. This underscores the importance of corporate governance mechanisms, such as the audit committee, in supervising financial reports and preventing actions that may harm the company, thus minimizing the risk of financial distress.

Research by Dwi Putra & Serly (2020) and Masak & Noviyanti (2019) indicates a negative correlation with financial distress. An increased frequency of audit committee meetings enables companies to more effectively identify and monitor their financial conditions, allowing the board of directors to make timely decisions before financial distress arises. Base on this finding, the following hypothesis can be formulated:

H2: The Audit Committee has a negative impact on the probability of financial distress.

Gender Diversity

Gender diversity refers to the representation of different genders in leadership roles, particularly on corporate boards. According to research by Fathonah (2018), gender is generally defined as a status shaped by social, cultural, and psychological factors based on individual characteristics. A study conducted by McKinsey in 2010 revealed that approximately 72% of directors acknowledged that the presence of women on the board could enhance company performance (Nurwahyudi & Mudasetia, 2020). The diversity of board members can impact a company's financial condition both in the short and long term. La Rocca et al. (2020) argue that cultural factors govern these behavioral differences. Given that the culture and traditions in Indonesia differ significantly from those of other countries, responsiveness, choices, and behavior are strongly influenced by the system used to assess problems. Therefore, the presence of gender diversity on corporate boards can foster a broader range of perspectives, helping to address financial issues and reduce the risk of financial distress. Companies that are managed by a variety of diversity, such as ethnicity, gender, and other cultural factors, show that boards of directors that have a greater percentage of similar cultural factors may prefer or not choose to express social responsibility as a legitimacy strategy to change the perceptions of other stakeholders (Surbakti & Sari, 2024).

Research by Rodiah & Kristanti (2021) and Abugri (2022) suggests that gender diversity has a positive influence on financial distress. In contrast, research by Anggriani & Rahim (2021) indicates that gender diversity has a negative impact on financial distress. Additionally, a study by Tri Arizka et al. (2021) proposes that gender diversity has no effect on financial distres. Based on these findings, the following hypothesis can be formulated:

H3: Gender diversity negatively impacts the probability of the interest coverage ratio.

Profitability

Profitability refers to a company's ability to generate profit from its transactions with customers. A systematic understanding of profitability is crucial for evaluating business strategies and making investment decisions. Profitability ratios are the most commonly used metrics for assessing a company's performance. Profitability is essential for a company's survival, as it will be challenging for the company to secure capital from external sources without profits.

This ratio measures the extent to which net income is generated from each unit of currency invested in total assets. A higher ratio indicates greater net profit generation, while a lower ratio suggests smaller profits. Profitability provides valuable insights into the profits earned by the company and their relationship to the company's stock value.

The relationship between net profit margin and financial distress is highlighted in research by Carmenita et al. (2023), which suggests that the risk of financial distress may increase when the net profit margin is low. This finding is consistent with the study by Nugraha & Fajar (2018), which indicates that net profit margin has a negative impact on financial distress. Base on these findings, the following hypothesis can be formulated:

H4: Profitability negatively impacts the probability of financial distress.

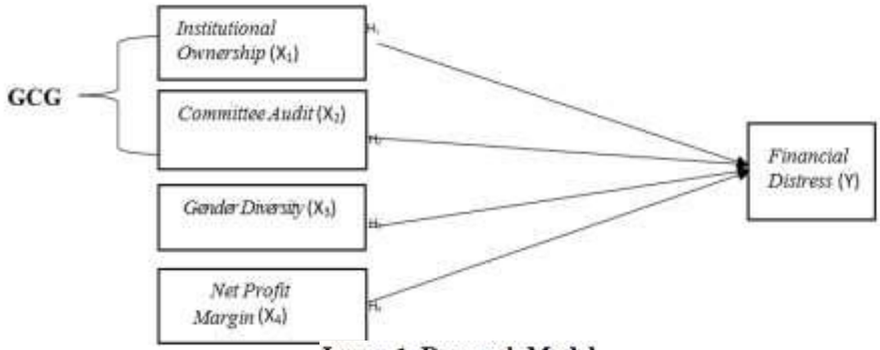

Image 1. Research Model

METHOD

This study adopts a quantitative approach with a population of non-cyclical consumer manufacturing companies listed on the Indonesia Stock Exchange from 2018 to 2022. The purposive sampling method is used, as samples are drawn based on specific criteria relevant to the research objectives, including companies that have complete financial and annual reports from 2018 to 2022 and are part of the non-cyclical consumer sector on the IDX. Data collection is conducted through secondary sources via company websites and annual reports on the IDX. Data analysis is performed using E-Views 12 with logistic regression.

Table 3.1 Operational Research Variables

Variable	Proxy	Formula	Scale
Financial Distress (Y) (Suranta et al., 2023)	ICR	$ICR = \frac{EBIT}{\text{Interest Expense}}$ The ICR method is used to classify companies into 2 categories: • Healthy (Category 0): Companies with an ICR value above 1, or do not have negative earnings for two consecutive years during the study period • Unhealthy (Category 1): Companies with an ICR value below 1, or those that have negative earnings for two consecutive years during the study period, indicating a risk of financial distress.	Dummy
GCG			
Institutional Ownership (X1) (Dirman, 2020a)	IO	$\frac{\text{Total of intitutional share}}{\text{Total of outsanding share}}$	Rasio
Audit Commite (X2) (Setiany et al., 2018)	AC	The number od meeting held per year	Rasio
Gender Diveristy (X3) (Fahlevi et al., 2023)	GD	$Blau\ Index = 1 - \left(\frac{BOD\ F}{Total\ BOD}\right)^2$	Rasio
Profitabilitas (X4) (J. Maulana & Suhartati, 2022)	NPM	$\frac{\text{Earning after tax}}{\text{sales}} \times 100\%$	Rasio

RESULT

This study focuses on manufacturing companies within the non-cyclical consumer sector from 2018 to 2022 that meet specific criteria. Initial purposive sampling identified 114 listed companies, From the total population, we identified 67 companies that met the predetermined selection criteria. However, only 51 of these companies had complete and accessible data for further analysis, resulting in a final sample size of 255 data points (51 companies over 5 years). A logit model was initially employed for regression analysis; however, due to the failure to meet assumptions in diagnostic tests, a probit model was subsequently selected to ensure the validity of the results.

Table 1 Descriptive Statistics Result

	FD	IO	AC	GD	PROF
Mean	0.5020	39.3116	5.8588	0.2605	-0.0561
Median	1.0000	31.5000	4.0000	0.3200	0.0200
Maximum	1.0000	96.8400	38.0000	0.5000	0.3400
Minimum	0.0000	0.0700	0.0000	0.0000	-2.7300
Std. Dev.	0.5010	29.3287	4.5032	0.1902	0.3549
Skewness	-0.0078	0.4588	3.8129	-0.3758	-4.7618
Kurtosis	1.0001	1.8268	22.3127	1.5568	31.0613

Source: Data processed using EViews, 2025.

Based on the calculations presented in Table 1, it can be observed that the research sample consists of 255 observations from 51 manufacturing companies in the non-cyclical consumer sector listed on the Indonesia Stock Exchange (IDX) during the period from 2018 to 2022, which meet the established criteria. The following information can be derived from this sample:
The average value (mean) is 0.5020, indicating that non-cyclical consumer companies from 2018 to 2022 have an average Interest Coverage Ratio (ICR) of less than 1, which shows that, on average, these companies experienced financial distress during this period. This suggests that the companies do not have sufficient cash flow and profits, making them unable to pay interest on their operating income. The ICR method and negative earnings are used to classify companies into two categories:

- **Healthy (Category 0):** Companies with an ICR value above 1, **or** do not have negative earnings for two consecutive years during the study period
- **Unhealthy (Category 1):** Companies with an ICR value below 1, **or** those that have negative earnings for two consecutive years during the study period, indicating a risk of financial distress.

Using this method, the researcher identified a total of 127 non-cyclical consumer companies classified as healthy and 128 as non-healthy, based on the analysis of the Interest Coverage Ratio (ICR) values, which indicated negative profits for two consecutive years during the study period. The average institutional ownership was 39.116, with a maximum value of 96.84 and a minimum value of 0.000, while the standard deviation was 29.3287. The average audit committee size was 5.858824, with a maximum value of 38.000 and a minimum value of 0.000, while the standard deviation was 4.503244. The average gender diversity score was 0.26051, with a maximum value of 0.500 and a minimum value of 0, while the standard deviation was 0.190212. The average profitability was -0.056078, with a highest value of 34.0 and a lowest value of -2.73, while the standard deviation was 0.3549130.

Hosmer and Lemeshow Test

Tabel 2 Hosmer and Lemeshow Test

H-L Statistic	14.6823	Prob. Chi-Sq(8)	0.0656
Andrews Statistic	30.1007	Prob. Chi-Sq(10)	0.0008

Source: Data processed using EViews, 2025.

Based on the results of the model adequacy test using the Andrews and Hosmer-Lemeshow Goodness of Fit Test, the Probability Chi-Squared H-L Statistic value is 0.0656, which is greater than 0.05. This suggests that the model employed is appropriate for use in this study.

McFadden R-squared

Tabel 3 McFadden R-squared Test

McFadden R-squared	0.466644	Mean dependent var	0.501961
S.D. dependent var	0.500979	S.E. of regression	0.343327
Akaike info criterion	0.778596	Sum squared resid	29.46842
Schwarz criterion	0.848032	Log likelihood	-94.27093
Hannan-Quinn criter.	0.806526	Deviance	188.5419
Restr. deviance	353.5011	Restr. log likelihood	-176.7506
LR statistic	164.9593	Avg. log likelihood	-0.369690
Prob(LR statistic)	0.000000		

Source: Data processed using EViews, 2025.

The McFadden R-squared value from the probit regression analysis is 0.466644 (46%), indicating that the variations in institutional ownership, audit committee, gender diversity, and net profit margin account for 46% of the variability in the interest coverage ratio. While the model demonstrates a relatively strong explanatory power, 54% of the variability remains unexplained, likely due to other factors that were not included in the study.

Z-Statistic Test

Tabel 4 Z-Statistic Test

Variable	Coefficient	Std. Error	z-Statistic	Prob.
C	1.518778	0.348508	4.357947	0.0000
IO	0.002207	0.003504	0.629859	0.5288
AC	-0.057579	0.036749	-1.566825	0.1172
GD	-3.591441	0.670342	-5.357622	0.0000
PROF	-13.74736	2.069194	-6.643824	0.0000

Source: Data processed using EViews, 2025.

The analysis of the z-statistic calculations and the probit regression equation is as follows:

1. The Probability z-statistic value is 0.5288. Compared to $\alpha = 0.05$, this probability is greater than α, leading to the decision to reject H1. Therefore, it can be concluded that institutional ownership does not affect financial distress.

2. The Probability z-statistic value is 0.1172. Compared to $\alpha = 0.05$, this probability is also greater than α, resulting in the decision to reject H2. This indicates that the audit committee does not affect financial distress.

3. The Probability z-statistic value is 0.0000. Compared to $\alpha = 0.05$, this probability is less than α, leading to the decision to accept H3. Thus, gender diversity has an impact on financial distress.

4. The Probability z-statistic value is 0.0000. Compared to $\alpha = 0.05$, this probability is less than α, resulting in the decision to accept H4. This demonstrates that net profit margin affects financial distress.

DISCUSSION

The first hypothesis (H1) suggests that institutional ownership does not influence financial distress, leading to the rejection of H1, which posits a negative impact. In other words, regardless of the proportion of institutional ownership in a company, the likelihood of experiencing financial distress remains unchanged. This implies that both higher and lower levels of institutional ownership do not affect financial distress, as measured by the interest coverage ratio. These findings contradict agency theory, which suggests that higher institutional ownership strengthens internal control, thus reducing agency costs. This control is expected to mitigate conflicts between principals (owners) and agents (managers), allowing owners to monitor managerial performance and preempt financial distress. However, this study did not find evidence to support this theory. The results are consistent with studies by Dirman (2020) and M. Maulana et al. (2020), which also found no significant impact of institutional ownership on financial distress. Conversely, these findings contradict those of Widhiadnyana & Dwi Ratnadi (2019) and Khan & Kong (2022), who suggested that higher institutional ownership negatively affects financial distress. A larger institutional shareholding can sometimes lead to actions that favor institutional interests over those of minority shareholders or the company as a whole.

The second hypothesis (H2) posits that the audit committee does not influence financial distress, leading to the rejection of H2, which assumes a negative impact. This suggests that variations in the frequency of audit committee meetings do not affect the likelihood of financial distress. Regardless of how often meetings are held, they do not prevent a company from experiencing financial difficulties. These results contradict agency theory, which argues that more frequent audit committee meetings enable management to identify unhealthy financial conditions more quickly and make timely decisions to prevent financial distress. However, the study found no significant differences between the meeting frequencies of companies that did and did not experience financial distress. One potential explanation for this lack of impact could be the competence of the audit committee, which is linked to members' educational backgrounds and their work experience in accounting or finance. This study’s findings align with research by Sukawati & Wahidahwati (2020) and Dwi Putra & Serly (2020), which also found no significant effect of meeting frequency on financial distress. In contrast, studies by Rachmawati & Rohman (2024) and Meidiyanti & Abdullah (2024) suggest that meeting frequency does influence financial distress, arguing that lower meeting frequencies may increase the risk of financial difficulties for companies.

The third hypothesis (H3) suggests that gender diversity negatively affects financial distress. The regression results support this hypothesis, leading to its acceptance. This study aligns with both the third hypothesis and agency theory, which posits that gender diversity on boards can influence the potential for financial distress. Managers or leaders with gender diversity are more likely to reduce conflicts of interest between principals and agents, particularly in risk management. The findings are consistent with research by Anggriani & Rahim (2021) and Abugri (2022), which indicate that greater gender diversity on boards is associated with a lower likelihood of financial distress. This is attributed to the tendency for women to make more cautious decisions, unlike men, who may be inclined to take higher risks. However, studies by Tri Arizka et al. and Samudra (2021) found no effect of gender diversity on financial distress, which could be due to the fact that high gender diversity does not guarantee the avoidance of financial difficulties. Effective decision-making depends heavily on the individual abilities of board members.

The fourth hypothesis (H4) suggests that profitability, as measured by the net profit margin, negatively affects financial distress. The regression results confirm that net profit margin does have an impact on financial distress, leading to the acceptance of H4. This finding is supported by research from Indrati & Putri (2021), which shows that the net profit margin reflects a company’s ability to generate net income from sales revenue. A higher net profit margin indicates greater effectiveness in profit generation, which helps companies manage financial distress. As profits increase, the likelihood of financial difficulties decreases. Thus, net profit margin can serve as a useful indicator for predicting financial distress. The better a company manages its revenue and expenses, the greater its ability to avoid financial distress. This finding aligns with research by Carmenita et al. (2023), which explains that a higher net profit margin enhances company performance and makes the firm more attractive to investors. This is consistent with agency theory, which posits that higher profitability aligns the interests of management (agents) with those of shareholders (principals), thereby reducing the risk of financial distress.

CONCLUSION AND SUGGESTIONS

Based on the problem formulation, research findings, and discussion, the conclusions drawn from this study are as: Institutional ownership does not influence financial distress. Regardless of the percentage of institutional ownership in a company, the probability of experiencing financial distress remains unchanged. The audit committee does not have an impact on financial distress. This suggests that variations in the frequency of audit committee meetings do not significantly influence the likelihood of financial distress. Gender diversity affects financial distress. A higher level of gender diversity on the board is associated with a lower probability of financial distress, as women tend to be more cautious in decision-making compared to men, who may be more inclined to take higher risks. Profitability influences financial distress. Higher profitability is linked to a reduced likelihood of financial distress, whereas lower profitability increases the likelihood of financial distress. In other words, there is an inverse relationship between profitability and the risk of financial difficulties for the company.

Based on these conclusions, the following recommendations are provided: **Future Research:** It is recommended that future studies extend the research period and incorporate additional variables, such as macroeconomic factors (e.g., inflation, taxes, exchange rates). Furthermore, broadening the focus to include other sectors listed on the Indonesia Stock Exchange or international exchanges such as the NYSE would provide valuable insights.

1. **For Companies:** It is advised that management implement robust corporate governance policies, improve profitability through operational efficiencies and product diversification, and adopt proactive risk management strategies to identify and address potential financial challenges at an earlier stage.
2. **Contribution to Society:** The public is encouraged to assess the financial performance of companies thoroughly when making investment decisions. In addition to financial metrics, it is important to consider non-financial factors such as the company's financial health and internal governance mechanisms.

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