CHAPTER II

CRITICAL LITERATURE REVIEW

2.1 Theoretical Literature Review

2.1.1 COVID-19 Pandemic

The COVID-19 – a genus in the *Coronaviridae* family – is a pleomorphic, enveloped virus. It is named after its typical crown-like appearance after seen through an electron microscope which contains glycoprotein spikes (Perlman & Netland, 2009). The World Health Organization that is cited on The Lancet (2020) research article mentioned that even though most of the infections of coronavirus on human are mostly mild, but the epidemics of the *Betacoronavirus* – namely the Severe Acute Respiratory Syndrome coronavirus (SARS-CoV) and the Middle East Respiratory Syndrome coronavirus (MERS-CoV) – have caused more than 10,000 cumulative cases with 10% of SARS-CoV mortality rates (2004) and 37% for MERS-CoV (2016). As an RNA virus, the Coronaviruses (CoVs) has the ability to infect immense range of animals, including humans, it causes respiratory, enteric, hepatic and neurological disease (Weiss & Leibowitz, 2011).

Yin and Wunderink (2018) in Di Gennaro et al., (2020) mentioned that the CoV's are classified into four groups based on their proteins sequence and phylogenetic relationships, namely: (I) α-CoV (*Alphacoronavirus*), (II) β-CoV (*Betacoronavirus*), (III) δ-CoV (*Deltacoronavirus*), and (IV) γ-CoV (*Gammacoronavirus*). The *Deltacoronvirus* and *Gammacoronavirus* may infect birds and mammals but have never reported to infect humans. While the *Alphacoronavirus* and *Betacoronavirus* are capable of affecting both humans' and animals' respiratory and gastrointestinal illness. Before December 2019, six common coronaviruses (that is part of *Alphacoronavirus* and *Betacoronavirus*) have infected human, those are: the HCoV-229E and HCoV-NL63 (belongs to *Alphacoronavirus*), HCoV-OC43 and HCoV-HKU1 (belongs to Lineage A *Betacoronavirus*), two deadly virus SARS-CoV and MERS-CoV belongs to the *Betacoronavirus* group Lineage B and C (Alanagreh et al., 2020).

Before the COVID-19 appeared, previous coronaviruses such as SARS-CoV transmitted to human through direct contact with the market of Civet cats (Ge et al., 2013). While MERS-CoV transmitted to humans through camels (Zaki et al., 2012). It is concluded that the seventh type of Corona Virus (2019-nCoV) is not a new type of virus, but is a result of mutation. The COVID-19 Virus stands for Corona Virus Disease that emerged at the end of year 2019, initially identified through several cases of pneumonia-like cases in Wuhan (Lu et al., 2020). Earlier in January 2020, it is identified that a novel virus is the causative agent towards the severe acute respiratory syndrome or known as the SARS-CoV-2 of the observed pneumonia groups (Huang et al., 2020). By March 11th 2020, the virus had reached 118,000 cases in 114 countries and caused 4,291 of deaths (WHO, 2020a).

2.1.2 Definition and Purpose of Multifinance Institution

The financing term is initially known as "leasing". Furthermore, the business field of finance companies is increasingly being expanded through the Presidential Decree Number 61 of 1988 concerning "Financial Institution" which was then followed up by the Decree of the Minister of Finance of the Republic of Indonesia Number 1251/KMK.013/1988 concerning Provisions and Procedures for implementing Financial Institutions.

The Indonesia Financial Services Authority (OJK) defines financing as the provision of money to finance debtor's needs in obtaining goods or services purchased through a third party (dealer/showroom/supplier) as a provider of goods or services based on a loan and loan agreement between the financing company and the debtor, which requires the debtor to pay-off his debt within a certain period of time along with interest and other fees charged (OJK, 2019). An analysis of Lim and Swandono (2017) mentioned that multifinance companies in Indonesia had contributed in bridging the gaps of those who don't have bank accounts. This unbanked population – both in urban and rural areas – certainly is an opportunity towards multifinance institution to provide the service of meeting financial needs of the lower income households. These type of customers are mentioned tend to have financing company preference that provide quick and easy services. Whereas it also supported government in combating the financial exclusion. It can be said that in terms of financial inclusion, Indonesia is left behind compared to other developing countries. As quoted in the analysis, the World Bank Survey in 2014 revealed that only 36% of adult population owned access in form of bank account to financial institution. While average Asia and Pacific Countries rated 69%, average of lower middle income countries rated 42%, and even Thailand as part of ASEAN rated by 78%. The percentage of adults who borrowed from financial institution is surprisingly only 13%. And as much as 42% of adult population prefers to borrow from friends or family. This unbanked population indicates of numerous untapped markets for lending in Indonesia. Another challenge for multifinance to penetrate is due to Indonesia's wide and unique geographical areas with underdeveloped infrastructure.

In the mid of 1974, the multifinance institution's focus is through leasing of heavy equipment to support national economy growth. Earlier in 1980's, the financing focus shifts to 2W (two-wheeled vehicles). Earlier in 2000's, the consumer spending increases. In 2014, the multifinance companies are officially allowed to finance multi-purpose loans, refinancing and infrastructure loan by the Financial Service Authority (OJK). Since then, the heavy equipment is no longer the driving force of multifinance growth, but the consumer financing do.

Therefore, it can be concluded that the Multifinance Institutions are companies that engaged in the finance industries and aimed at providing loan-financing service.

2.1.3 COVID-19 and Economic Growth

Global Economy

The risk of global economy increased in the midst of COVID-19. Massive impacts are estimated to be emerged towards the global economics. The Organization for Economic Cooperation and Development (2020) estimated global economic growth; by 2.4% if the pandemic peaks by the end of the first quarter of 2020, and by 1.5% if the pandemic scattered intensively and worsen throughout Asia Pacific region, Europe, and the United States. Another impact of the pandemic is the high volatility in the global financial sector as seen from the increase in the VIX index (the highest level since the Global Financial Crisis 2008) and the increasing demand for *safe haven assets* such as gold, US securities and US Dollar. The price of crude oil commodities also fell sharply amid fears of falling world demand coupled with the disagreement of Russia and Saudi Arabia in reducing crude oil production.

Monetary authorities in the world decreased interest rates to stimulate the economy. By March 2020, the Fed has twice lowered the Fed Funds Rate to the level of 0.0 – 0.25%. Fiscal support was also carried out by other countries, especially directed at supporting health programs in the context of handling COVID-19, maintaining public consumption, and supporting the affected sector.

National Economy

The economic growth comparison of the first quarter between 2019 and 2020 appeared to fell from 5.07% to 2.97% (YoY) (BPS, 2020a). The economic growth is mainly driven by GDP and the slowdown is driven by consumption reduction. All sectors experienced a slowdown due to the falling of global and domestic demand aligned with the declining of international commodity prices. Indonesia’s Real GDP Growth experienced a slowdown from 5% (YoY) in Q4 2019 into 3.1% (YoY) in Q1 2020 which is mentioned by the World Bank as the lowest quarter growth since 2001. This disadvantageous global economic condition is then aggravated by a crumbling economic activity as the Indonesian Government implemented Large-scale Social Restrictions in March and continuously the partial lockdown from April to June.

Consumption growth experienced a sharp fall from 4.2% (YoY) in Q4 2019 into 2.8% in Q1 2020. Private consumption growth dropped from 4.9% (YoY) in 2019 into 2.7% (YoY) in Q1 2020. Otherwise, government consumption increased by 3.7% (YoY) in Q1 and is the only category with positive increment, aligned with the growth of health sector which grew by 10% due to the high-spread of the COVID-19. Fixed investment growth fell steeply from 4.1% (YoY) in Q4 2019 into 1.7% (YoY) in Q1 2020 (World Bank, 2020). Indonesia's main export commodities such as crude oil, palm oil, coal, rubber, liquefied natural gas and base materials contracted on average by 8.9% (YoY) in Q1 2020 (Reuters, 2020). Building and structures growth fell as investors postponed projects, the percentage of fall is from 5.5% (YoY) in Q4 2019 into 2.8% in Q1 2020. Leading indicators of investments had given signals of downturns in Q2. Indonesia's Purchasing Manager's Index (PMI) for manufacturing plunged to its lowest record of 27.5 in April (Trading Economics, 2020). Exports of goods and services growth is contracted from 0.4% in Q4 2019 into 0.2% in Q1 2020. Meanwhile, import volumes dropped to 2.2% in Q1 2020, after a decrease of 8% in Q4 2019. Continuously, Indonesia's economic growth in Q2 is contracted until 5.3% (YoY) which is the worst since 1998 monetary crisis (Bappenas, 2020).

To tackle the impact of COVID-19, the Government had taken steps through refocusing on budgeting for health sector and social assistance. The refocusing action is through the reallocation of the Ministry budget amounting Rp. 5 – 10 trillion. In the midst of the ongoing pressure, the 2020 State Budget will continue to give priority to handling COVID-19. The government had also optimized fiscal instrument to mitigate pressures that occurs. Two stimulus packages are launched; volume I amounting Rp. 8.5 trillion aimed at directly-affected sectors, and Volume II which is aimed at maintaining people's purchasing power and consumption, especially the lower classes, and prevent business bankruptcy, including MSMEs (Kementrian Keuangan, 2020).

2.1.4 Monetary and Banking Development

The Statistical Department of *Bank Indonesia* (2019) mentioned that the monetary condition of the economy by the end of 2019 showed an improved liquidity compared to the situation by the end of 2018. The economic liquidity development of early 2020 is slightly improved compared to 2019. In the meantime, until March 2020 liquidity in financial market that is shown through the action of lowering interbank money market rates (PUAB) and JIBOR rates is preserved.

The rate of money supply growth slightly increased; M1 from 7.1% in 2019 to 7.9% YoY in 2020, and M2 from 6.5% in 2019 to 7.1% YoY in 2020. M1 and M2 showed another increment by January 2020 into 7.9% and 7.1%. The increase in money supply (M1) was mainly due to growth in currency, while the increase in M2 growth was driven by the increase of net foreign assets. On the other side, net domestic assets grew at a slower pace, in line with slowing lending and contraction in government financial operations (Kementerian Keuangan, 2020b). Due to the economic pressure, the BI Board of Governors on a press release on February decided to decrease the BI 7-day Reverse Repo Rate by 25 bps from 5.0% to 4.75%, Deposit Facility decreased by 25 bps to 4.00%, and Lending Facility decreased by 25 bps to 5.50%. These actions are taken to control inflation to remain in its target corridor, maintaining stability, and to promote economic growth (Bank Indonesia, 2020a).

However, the banking credit development in early 2020 remains a challenge towards the performance of the domestic economy, particularly in relation to the relatively slow credit growth. The banking credit loan in December 2019 reached 5.9% YoY and is decreasing in the following January 2020 which reached 5.7% YoY. Certain factors came from demand and supply which could affect credit loan growth; corporations tend to withhold credit demand align with the downtrends of export performance and non-building investing activity. While on the supply side, banks tend to be extremely precautious in supplying credits in the midst of global uncertainty which is possibly affecting the domestic corporate performance (Bank Indonesia, 2020b).

The growth rate of the *Third-party Fund* that performed as the bank's main source of fund as per-January 2020 reached 6.8% YoY, slightly higher than the previous month that reached 6.5% YoY. The increasing of the *Third-party Fund* amidst slowing credit growth has led to a decrease in *Loan to Deposit Ratio* from 93.9% in December 2019 into 92.8% in January 2020. It is hoped that through the decreasing of LDR may give more space for banks to boost their credit expansion. Problems that needs to be highlighted in terms of a low acceleration of banking credit are; (1) Low credit demand from real sectors align with the arising global uncertainty and weakened economic activity, (2) a very slow pace of banking credit source of funds, mainly that came from third-party fund, (3) how banks manage their liquidity through credit distribution to limited and credible debtors, and (4) a very slow credit interests.

Generally speaking, the banking performance as of January 2020 was dominated by trade and manufacture sector. It is also mentioned that banking performance by January 2020 had booked *Net Interest Margin* (NIM) of 4.96%, slightly higher compared to January 2019 that reached 4.92%. In terms of banking *Capital Adequacy Ratio* (CAR) attained 22.83%, which is far from the minimum limit of 8% settled by *Bank for International Settlement* (BIS). Nonetheless, the impact of COVID-19 is more pronounced towards the banking credit quality that is seen from an increase in *Non-Performing Loan*

(NPL) from 2.04% in December 2019 into 2.19% in January 2020 (Kementerian Keuangan, 2020a).

2.1.5 Effects on Multifinance Institution

In 2020, the Multifinance industry is faced with overwhelming challenges. This pandemic has weakened new financing requests and restructured financing affected to COVID-19. The sluggish economic situation had forced the Multifinance institution to collect and issued their reserves which continuously increased their efficiency ratio. It is clearly seen from an increased in their *Operating Expense to Operating Income* (BOPO) from 79.15% per-August 2019 to the level of 91.95% per-August 2020. In the following month of September 2020, the efficiency of Multifinance institution expressed in BOPO increased to the level of 107.09% (Kontan, 2020a).

Aside from that, the *Financing Receivables* growth per-August 2020 recorded entirely deep contractions that reached -12.86% YoY and *Non-Performing Financing* (NPF) by 5.2% (Kontan, 2020b). Financial Service Authority (OJK) data recorded that the realization of Multifinance financing experienced a downturn value by 12.86% YoY from Rp. 449.80 trillion per-August 2019 to Rp. 391.96 trillion per-August 2020 (Kontan, 2020a). In the following month, the *Financing Receivable* is corrected by 17.1% YoY into Rp. 375.91 trillion on November 2020 and is dominated by the multipurpose financing. It reached Rp. 225.37 trillion or contributed 59.95% of the total industry financing (Kontan, 2021b). The object of the multipurpose financing is majorly motorized vehicle, both two-wheeled and four-wheeled. The Association of Indonesia Motorcycle Industry (2020) statistics have shown a decrease of motorcycle sales which is detailed by decreasing domestic sales by 44% and exports by 14% compared to the previous year of 2019. While the Association of Indonesia Automotive Industries (2020) declared a decrease of car sales by 48% in 2020 compared to 2019. The decline of financing is partially as the impact of the large-scale restriction (PSBB) imposed by the government and the declining of debtors' ability to pay which caused Multifinance institutions to be more selective in distributing credits (Kontan, 2021a).

Until October 2020, the Financial Service Authority (OJK) has received a restructuring requests of 5.4 million contracts from a total of 181 Multifinance Institutions with an outstanding principal of Rp. 166.66 trillion and interests of Rp. 42.43 trillion. Agreed contracts reached 4.79 million of contracts with the amount of outstanding principals of Rp. 140.25 trillion and interests of Rp. 37.41 trillion. Contracts in progress of restructuring amounted 307.840 contracts with total amount of outstanding principals of Rp. 11.44 trillion and interests of Rp. 37.41 trillion. Meanwhile, contracts with criteria-unmatched requests reached 301.641 contracts with total amount of outstanding principals of Rp. 9.98 trillion and interests of Rp. 2.54 trillion (Kontan, 2020c).

2.1.6 Rentability

Rentability is an assessment towards the ability of Multifinance Institution to generate profit (OJK, 2016). It is measured through four ratios, and each ratio weighted 25%.

2.1.6.1 Return on Asset (ROA)

ROA is the ratio used to measure the ability of Multifinance Institution to generate profit through the usage of asset to support the operational and capital of Multifinance. The formula of ROA is as follows:

$$\text{ROA} = \frac{Profit\ or\ Loss\ Before\ Tax}{Total\ Asset}$$

Source: OJK (2016)

2.1.6.2 Return on Equity (ROE)

ROE is the ratio used to measure the ability of Multifinance Institution to generate profit from its equity. The formula of ROE is as follows:

$$\text{ROE} = \frac{(Net\ Profit\ or\ Loss)}{Average\ Equity}$$

Source: OJK (2016)

2.1.6.3 Operational Expense to Operational Income (BOPO)

BOPO is the ratio used to measure the Multifinance Institution's level of efficiency and its ability to carry out its operational activities. The formula of BOPO is as follows:

$$\text{BOPO} = \frac{Operational\ Expense}{Operational\ Income}$$

Source: OJK (2016)

2.1.6.4 Net Interest Margin (NIM)

NIM is the ratio used to measure the Multifinance Institution's ability in managing its financing receivables to generate net interest income. The formula of NIM is as follows:

$$\text{NIM} = \frac{\textit{Net Interest Income}}{\textit{Average Financing Receivables}}$$

Source: OJK (2016)

2.1.7 Quality of Financing Receivables

The quality of financing receivables is an indicator of whether the financing provided to the consumers (debtors) will be paid in a timely manner through monthly installments. According to OJK (2016), the assessment of quality of financing receivables are categorized to five:

No	Category	Sidelight
1	Fluent	If there is no delay or there is delay in payment of principal and/or interest up to 30 calender days.
2	Under Special Attention	If there is a delay in payment of principal and/or interest that had exceeded 30 to 90 calender days
3	Substandard	If there is a delay in payment of principal and/or interest that had exceeded 90 to 120 calender days
4	Doubtful	If there is a delay in payment of principal and/or interest that had exceeded 120 to 190 calender days

5	Not Fluent	If there is a delay in payment of principal and/or interest that had exceeded 180 calender days

Table 2. 1 - Quality of Financing Receivables Assessment Category

The quality of financing receivables are considered as non-performing financing (NPF) if they are substandard, doubtful, and not fluent. The formula of NPF is:

$$\text{NPF} = \frac{NPF - Allowance\ For\ Write\ \text{off of Financing Receivables}}{Total\ Financing\ Receivables}$$

Source: OJK (2016)

2.2 Conceptual Framework

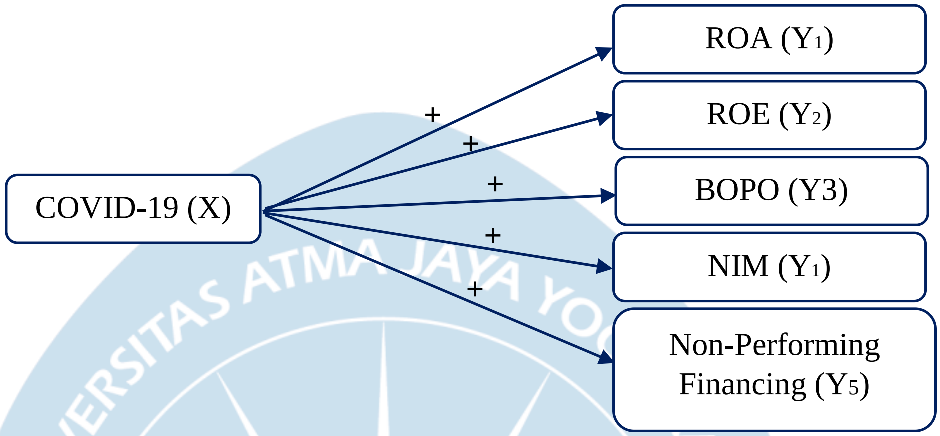

Figure 2. 1 - Conceptual Framework

2.3 Previous Research

Shen (2020a) researched about "The Impact of the COVID-19 Pandemic on Firm Performance". This research comprehensively discussed the impact of COVID-19 pandemic on corporate performance. The research divided the listed companies into high- and low-affected groups by region and industry dimension. The research used Difference-In-Differences (DID) model to quantify the impact of COVID-19 on firm performance. Investment growth and total revenue is used as moderating variable. The research focused on the regression coefficient. It is found that COVID-19 reduced corporate revenues which led to lower performance. It is also found that the COVID-19 outbreak resulted in a decline of corporate performance, both in industry and region dimension. More investment and income would effectively reduce the negative impact of the pandemic.

No	Title of Journal	Author	Name of Journal	Problem of the Research	Hypothesis	Result
1.	The Impact of the COVID-19 Pandemic on Firm Performance	1. Huayu Shen 2. Mengyao Fu 3. Hongyu Pan 4. Zhongfu Yu 5. Yongquan Chen	Emerging Markets Finance and Trade	Investigated the impact of COVID-19 on corporate performance, explored the mechanisms in which COVID-19 affect corporate performance	H1-1: *Ceteris Paribus*, COVID-19 has a negative impact on the performance of listed companies. H1-2: *Ceteris Paribus*, when the firm's investment is smaller, the negative impact of COVID-19 on the firm performance is more pronounced. H1-3: *Ceteris Paribus*, the negative impact of COVID-19 on firm performance is more pronounced,	It is found that COVID-19 reduced corporate revenues which led to lower performance. It is also found that the COVID-19 outbreak resulted in a decline of corporate performance, both in industry and region dimension. More investment and income would effectively reduce the negative impact of the pandemic.

					if a firm's sales revenue is less. H2: *Ceteris Paribus*, the COVID-19 Pandemic has a negative impact on the performance of enterprises in serious-impact industries. That is, the enterprises in serious-impact industries have lower performance than those in the other industries, following the pandemic. H3: *Ceteris Paribus*, the COVID-19 Pandemic has a negative impact on corporate performance in the serious-	

					impact regions. That us, corporate performance in the serious-impact regions is lower than in other regions.	

Table 2. 2 - Previous Research

2.4 Hypothesis Development

1. ROA is the ratio used to measure the ability of Multifinance Institution to generate profit through the usage of asset to support the operational and capital of Multifinance. However, COVID-19 disruption may have caused financial pressures included ROA.

   Based on the description above, the hypothesis is formulated as follows:

   H1 = **There is a difference of Multifinance Institution's *Return on Asset* (ROA) before and during COVID-19.**

2. ROE is the ratio used to measure the ability of Multifinance Institution to generate profit from its equity. However, COVID-19 disruption may have caused financial pressures included ROE.

   Based on the description above, the hypothesis is formulated as follows:

H2 = **There is a difference of Multifinance Institution's *Return on Equity* (ROE) before and during COVID-19.**

3. COVID-19 is an infectious major health emergency worldwide that infected more than seven million people until January 2020. Countries' policy responding to COVID-19 including Indonesia is by imposing self-quarantine due to the virus' highly infectious nature. Multifinance Institution are forced to issued their reserves due to weakened financing request had consequently increased efficiency ratios that indicates the inability and ineffectiveness of managing its operational expense.

   Based on the description above, the hypothesis is formulated as follows:

   H3 = **There is a difference of Multifinance Institution's *Operational Expense to Operational Income* (BOPO) before and during COVID-19.**

4. NIM is the ratio used to measure the Multifinance Institution's ability in managing its financing receivables to generate net interest income. However, COVID-19 disruption may have caused financial pressures included NIM.

   Based on the description above, the hypothesis is formulated as follows:

   H4 = **There is a difference of Multifinance Institution's *Net Interest Margin* (NIM) before and during COVID-19.**

5. The measures responding to COVID-19 had also given great negative impact on Multifinance Institution in terms of the Quality of Financing Receivables. At this point, the confidence level of lenders and customers weakened. In times of COVID-19 Pandemic, economies are creamed and consequently creates a situation of weakened financing requests and restructured financings due to inability of meeting short-term payments.

   Based on the description above, the hypothesis is formulated as follows:

   H5 = **There is difference of Multifinance Institution's *Non-Performing Financing* (NPF) before and during COVID-19.**