SUMMARY

IRMA OKTIANI. Determinants of Financial Soundness and Profitability of Life Insurance Companies in Indonesia. Supervised by DS. PRIYARSONO and TRIAS ANDATI.

Financial analysis is an important tools for insurance companies to evaluate and develop business strategies. The insurer's financial soundness and profitability are two financial ratios that have an important role to the life insurance business. The ratio of financial soundness proxied by the Risk Based Capital (RBC) ratio and is a ratio that is closely monitored by regulators (Financial Services Authority). Profitability ratio proxied by the Return On Assets (ROA) ratio and is a ratio that concerns the management of life insurance companies.

The development of life insurance industry in Indonesia as seen from the financial soundness and profitability has fluctuated from 2010 to 2014. This is a result of the global and national economic crisis. Uncontrolled fluctuations will have a negative impact on the development of national life insurance industry. An understanding of the determinants of the level of the financial soundness and profitability should be owned by companies and regulators to formulate business strategies and to encourage the growth of national life insurance industry. In developing countries, such as Indonesia, the empirical studies on the determinants of financial soundness and profitability of life insurance companies as a whole, has not been done. Therefore, the purpose of this paper is to analyze the characteristics and determinants of financial soundness and profitability of life insurance companies in Indonesia from 2010 to 2014. In order to answer these objectives, this study used two models (RBC model and ROA model). Factors to be considered will affect the financial soundness (RBC model) is the composition of its assets, such as the proportion of assets invested in stocks, bonds, mutual funds, securities and depositsaccompanied with macroeconomic variables such as inflation rate and interest rates. Factors to be considered in the analysis of determinants of profitability (ROA model) are derived from the company-specific factors, such as liquidity ratio, leverage ratio, risk-based capital ratio (RBC), equity capital, size of company, premium growth and macroeconomic factors, inflation. Both were analyzed with panel data regression methods and processed using the software E-Views 9.

The results of the panel data analysis produced some findings, namely (1) panel data regression using fixed effects model (FEM) in RBC model show that the R^2 in this research is about0.7766. It means about 77.66 percent variation of RBC can be explained by the variation of independent variables, while 22.34 percent is explained by other variables outside the model. The mean value of RBC ratio of life insurance companies was 558.70 percent, far above the minimum required by the FSA (120 percent) and indicates that the financial soundness of insurance companies in Indonesia need to be controlled by the FSA because it can be a negative effect on profitability (ROA) of life insurance companies, (2) regression of data panel using a fixed effect model (FEM) in ROA model provides adjusted R^2about 0.8435. It meansthat about 84.35 percent ROA variation can be explained by the independent variables use in model, while about

15.65 percent is explained by other variables outside the model. Variables that have positive and significant effect on ROA are size of company, equity capital, leverage ratio and liquidity ratio at 75 percent confidence level. Variables that have significant and negative effect is premium growth dan RBC, while inflation is statistically insignificant.

The results showed that the regulators should be supervising the financial soundness and also the composition of assets of the investment made by life insurance companies, so that will not cause bankcruptcy. In addition, life insurance companies in larger scale will have a better level of profitability compared with small companies. The results of this study can be used as the base material consideration of the regulator to tighter supervision of the financial soundness of insurance companies and also for management in managing the business strategy to improve profitability and can be used by prospective policyholders to choose a life insurance company that is reliable.

Keywords: asset composition, company-specific factors, financial soundness, macroeconomics, profitability