

Influence of Non-Performing Loans and Interest Rates on Company Profits with Profitability Levels as Intervening.**Annisa Azzahra¹, Hendra Gunawan¹, Syauki Aditya¹, Muhammad Irfan Nasution¹**¹Universitas Muhammadiyah Sumatera Utara

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*Email: annszhr8@gmail.com**ABSTRACT**

This research aims to acknowledge the influence of non-performing loans and interest rates on company profits with profitability levels as intervening in a Case Study at PT. BPR DUTA ADIARTA Medan. The approach of this research is quantitative method and uses SmartPLS. The sample of this research is the financial reports of PT. BPR Duta Adiarta Medan. The sources of data in this research is using secondary data, obtained from the internal of the sub-banking financial sector company. The method used in this research are data collection and analysis of reports. The analysis results shows three accepted hypotheses, which are the influence of non-performing loans towards profitability levels, influence of non-performing loans towards company profits, and the influence of interest rates towards company profits. The two denied hypotheses are the influences of interest rates towards profitability levels and the influence of profitability levels towards company profits.

Keywords : Non-Performing Loans, Interest Rates, Profitability Leves, Company Profits.

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INTRODUCTION

PT. BPR Duta Adiarta is a company engaged in the banking sector that manages finances in the public credit field. Offered services are providing loans to customers as capital or for consumption needs. BPR Duta Adiarta was founded in 2003 with thousands of customers, particularly in Medan. BPR Duta Adiarta helps small and medium enterprises and people who need fast funds. Engaging in the finances poses a risk of loss for the company, thus the loans provided are guaranteed by LPS (Lembaga Penjamin Simpanan or Indonesia Deposit Insurance Corporation) Institution and supervised by OJK (Otoritas Jasa Keuangan or Financial Services Authority) Institution. In a corporation, the company's management regulates the level of taking or loss. Obtaining optimum profits depends on how the management deals with existing risks.

The purpose of this research is to analyse the causal factors of non-performing loans and other problems that are frequently faced by the company. X variable (Non-performing loans and interest rates) are closely related to the Y variable (profitability levels), influencing efficient profits generated in the Banking Industry at PT. BPR Duta Adiarta Medan. A Non-performing loan (NPL) is a condition where credit return approval is at risk of failure. NPL shows bank management capability to manage NPL provided by the bank. The higher the NPL is, the worse the quality of the bank will be, resulting in an increased number of credits. In banking management, the increase in non-performing loans might cost the bank to lose its ability to produce optimum profits.

Optimum profits are the purposes of all companies, but it depends on how the management works. Therefore, banks started to acknowledge that customer selection is influential in avoiding non-performing loans. The issue of non-performing loans has become an increasing concern in recent years because the number has increased, which causes problems that can reduce bank operating income. The bank's operational income can become smaller due to non-performing loans or bad loans, and it is also discovered that banks charge relatively higher interest rates, where excessive lending will lead to higher levels of non-performing loans (Akter & Roy, 2017).

Interest rates have raised concerns about monetary policy continuously. Negative interest rates can induce lower profitability, causing expansive monetary policy contraction, and if the interest rates are too low for the long term, the bank is persuaded to take risky credits. It is proof that there is nothing special regarding negative interest rates (Urbschat, 2018). Interest rate is one of the essential factors that influence financial ability. Interest rates are the price borrowers pay to the lenders for the money they lend, or the price paid for the borrowed assets (Crowley, 2007). Meanwhile, financial performance is defined in terms of probability, where probability itself is a company's ability to obtain a reasonable profit on the owner's investment, therefore financial performance is very crucial for operational activities because it is necessary to understand the various determinants of interest rates and their impact on performance. (MAIGUA & MOUNI, 2016). The relationship between bank profitability and low-interest rate in the long term generally negatively impacts the bank's profit. Banks can compensate for lower loan interest by decreasing their funding interest rates. However, the funding rate is limited to a lower bound of zero, as customers are not expected to receive negative deposit rates. Profit margins are removed along with net interest margins, and since bank profits largely determine a bank's capital, lower profit margins can put pressure on a bank's capital position and thus on its solvency. This should also be seen given the tighter capital requirements (Bikker & Vervliet, 2018).

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Regarding the previous variables, interest rates and non-performing loans, greatly determines or have an impact on profits. Profits are the final amount of wealth that can be distributed to shareholders within a certain period of time (Hassoune, 2002). In conclusion, profits can be influenced by interest rates and non-performing loan variables. Companies should strengthen their management on managing interest rates and credit accordingly to avoid company loss because factors of the variables are high risks, and the consequences are significant losses. The increasing potential of non-performing loans can oppose difficulty for the bank in the intermediating finance process, which strongly impacts the company's liquidity and profitability (Bolat & Isik, 2016).

Interest rates can significantly affect the company, even the stability of the nation's economy. The effect of the interest rate itself is, if you experience low-interest rates, the company can help economic recovery and improve the balance sheet and company performance by generating capital gains and reducing non-performing loans, but low-interest rates that are continuously low in the long term can causing erosion of the profitability and value of a bank or company franchise. Because interest rates are usually associated with lower net interest margins (Claessens et al., 2017).

Developing countries such as Indonesia, rely heavily on the banking industry for financial intermediation. Companies or banks contribute to economic growth by giving out effective and efficient loans. NPL is the current problem in the banking sector, with increasingly ineffective loans, according to (Sazzad et al., 2019a) non-performing loan is an irregular loan whose interest and product amount are due for a certain period of time. An increase in NPL can pose a threat to financial ability, also decreasing profits and loan capacities by decreasing the company's assets. According to (Choudhary, 2017) NPL is a loan where the loan does not make payments following the contractual obligations. NPL is also defined as the amount of loan money in which the debtor has not made scheduled payments for at least 90 days (Bholat et al., 2016). Reducing non-performing loans in the long term gradually affects profitability (Kaaya & Pastory, 2013a). The risk is that problem loans usually result in high credit reserves causing a decrease in profits (Kithinji, 2010a), and gradually minimize the banking sector's ability to take part in economic growth (Karim et al., 2010).

(Million et al., 2015) emphasized that NPL is the primary indicator of credit risk, with the founding that NPL has significant great negative effects statistically towards profitability measured using ROA. However, (Li & Zou, 2014) and (Alshatti, 2015) found that NPL positively affects financial ability.

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Table 1. Data

ANNUAL REPORT ON NPL, INTEREST RATES, PROFITABILITY AND PROFIT RATES								
PT. BPR DUTA ADIARTA MEDAN								
2015-2022								
YEAR	NET PROFING LOAN	(%) HIGH/LOW	INTEREST RATE	(%) HIGH/LOW	PROFITABILTY RATIO	(%) HIGH/LOW	NET PROFIT	(%) HIGH/LOW
2015	2.366.958.772	-	21%	-	3,20%	-	Rp 1.366.314.276	-
2016	1.317.878.697	-44,32%	21%	-	5,14%	60,63%	Rp 1.581.944.854	15,78%
2017	977.502.143	-25,83%	20%	-4,76%	6,25%	21,60%	Rp 2.157.569.082	36,39%
2018	1.575.430.075	61,17%	20%	-	5,32%	-14,88%	Rp 1.972.058.903	-8,60%
2019	1.650.289.139	4,75%	20%	-	5,45%	2,44%	Rp 2.177.487.515	10,42%
2020	980.755.122	-40,57%	20%	-	5,85%	7,34%	Rp 1.593.593.581	-26,82%
2021	892.765.908	-8,97%	20%	-	6,41%	9,57%	Rp 2.053.920.475	28,89%
2022	803.045.789	-10,05%	20%	-	6,87%	7,18%	Rp 2.321.678.092	13,04%

Based on the table above, we use data on non-performing loans, interest rates, profitability levels and net profit of PT. BPR Duta Adiarta for the last 8 years to see the level of influence of bad loans and interest rates on net income and the level of profitability as intervening variables. Based on the table above, we use data on non-performing loans, interest rates, profitability levels and net profit of PT. BPR Duta Adiarta for the last 8 years to see the level of influence of bad loans and interest rates on net income and the level of profitability as intervening variables. From the analysis of the table above, it can be seen that the phenomenon occurred in the 2017 income statement, where the interest rate decreased by 4.76% to 20% per year from the reduction in interest in the previous year of 21%, made the profit earned in 2017 increase by 36.39% from the previous year, and non-performing loans (NPL) in 2017 decreased by 25.83% from total non-performing loans in the previous year, and the level of profitability in 2017 increased by 21.60% from the previous year. The phenomenon above is used as a sample that the theory of non-performing loans and interest rates affect the profits earned by the company and increase the level of profitability obtained by the company.

The most profit obtained from 2015-2022 is in 2022 with a total profit of Rp. 2,321,678,092 with the lowest total bad loans from previous years of Rp. 803,045,789. This is greatly influenced by the company's management in managing and providing credit to the public in order to reduce the number of non-performing loans from 2015-2021 and obtain maximum profits.

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The interest rate in 2015 and 2016 was 21%, which resulted in a significant impact on the company's profit, which was also the year when the number of non-performing loans was very high. According to the table, in 2015, the total non-performing loans were far more than the profits generated by the company that year. This might be triggered by several factors including the influence of high-interest rates, handling of non-performing loans that are ineffective and inefficient, as well as internal company factors such as the company's operational costs in that year.

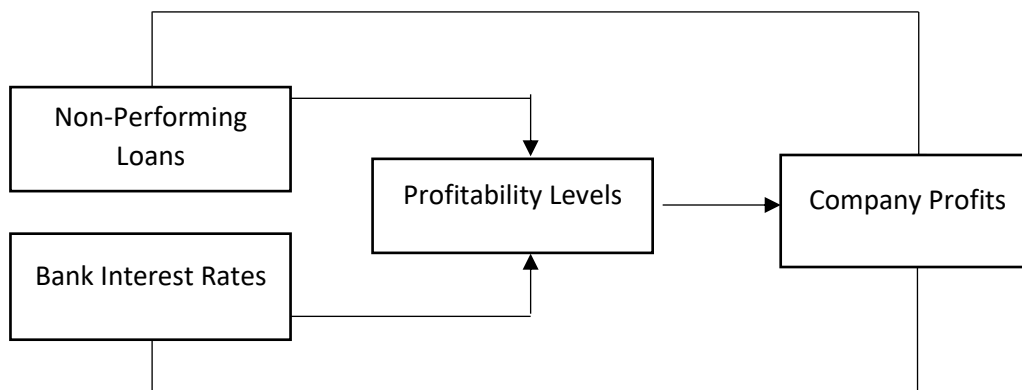


Figure 1. Conceptual Framework

In the conceptual framework above, the hypothesis obtained is: H1: There is a significant relationship between non-performing loans and the level of profitability which can affect profits generated efficiently. The existence of non-performing loans, of course, hinders the company from obtaining profits. H2: Interest rates and the effect of inflation are closely related to obtaining the desired level of profitability because it attracts depositors or investors to invest in the company. H3: The profit desired by the company is influenced by the turnover of capital and loans given to customers. Good management is needed in minimizing the risk of loss. H4: Sector or country's economic conditions affect interest rates in banks.

METHOD

According to the title, variables that will be analysed are non-performing loans, interest rates, profitability levels, and company profits of PT. BPR Duta Adiarta Medan. Researchers used secondary data sources obtained from the internal of the sub-banking financial sector company. The sample of this research is PT. BPR Duta Adiarta Medan. The approach of this research is quantitative method and used SmartPLS3. the quantitative approach emphasizes testing theories or hypotheses by measuring research variables in numbers and conducting data analysis using statistical procedures. The data collection uses documentation techniques by taking documentation of related company financial statements.

RESULT AND DISCUSSION

After the financial data regarding total bad loans, interest rates, profitability and company profits from 2015-2022, the validity and reliability values obtained are as follows :

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Table 2. Validity and reliability construct

Variable	Cronbach's Alpha	rho_A	Composite Reliability	Average Variance Extracted (AVE)
Net Profing Loan (X1)	1,000	1,000	1,000	1,000
Interest Rate (X2)	1,000	1,000	1,000	1,000
Profitability Ratio (Z)	1,000	1,000	1,000	1,000
Net Profit (Y)	1,000	1,000	1,000	1,000

The Composite Reliability and Cronbach Alpha test results also show valid values, namely reliable latent variables because all latent variable values have Composite Reliability and Cronbach's Alpha values of > 0.70 (Table 1). The next test is discriminant validity. A construct is considered to have good discriminant validity if each loading factor value for each latent variable indicator has a very significant loading factor value with other loading factor values for other latent variables

Results of Sub-Structural Research I

It can be seen in the indicators of non-performing loans, interest rates, profitability levels, and company profits that the Latent construct predicts indicators in its part to be better than indicators in other parts.

Table 3. Discriminant Validity Test Result (Cross)

Net Profing Loan (X1)	Interest Rate (X2)	Profitability Ratio (Z)	Net Profit (Y)
0,483	1,000	-0,310	-0,619
-0,602	-0,310	1,000	0,475
1,000	0,483	-0,602	-0,707
-0,707	-0,619	0,475	1,000

Results of Sub-Structural Research II

The results of convergent validity testing on several indicators have been fulfilled because all loading factor values are above 0.70. So, this reflects that all indicators are valid. In addition, the AVE value must be above 0.5. The results of reliability and construct validity show a valid AVE value (Table 1).

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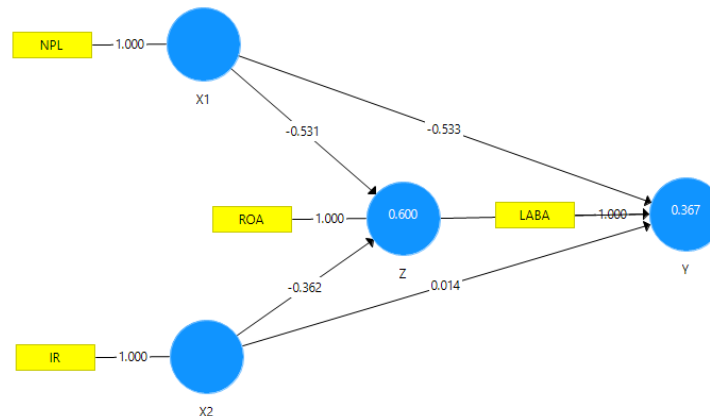


Figure 2. Structural Model (Inner Model)

Sobel Test

Table 4. Hypotheses test results (Path coefficients)

	Original Sample (O)	Sample Average (M)	Standard Deviation (STDEV)	T Statistic (O/STDEV)	P Values	Note
Non-Performing Loans -> Profitability Levels	-0,533	-0,473	0,151	3,531	0,001	Accepted
Non-Performing Loans -> Company Profit	-0,531	-0,573	0,155	3,432	0,002	Accepted
Interest Rates -> Profitability Levels	0,014	-0,044	0,154	0,088	0,930	Rejected
Interest Rate -> Company Profit	-0,362	-0,339	0,156	2,328	0,027	Accepted
Profitability Levels -> Company Profit	0,106	0,117	0,216	0,493	0,626	Rejected

Explanation from the table is as follows: Non-performing Loans towards Profitability Levels. Based on the table with path analysis, it can be seen that the path coefficient value is 0.646 with a T-statistic of 3.531 > 1.96. Because the significance is <0.05, the H1 hypothesis is accepted. Based on the table with path analysis, the effect of non-performing loans on company profits with a T-statistic value of 3.432 > 1.96. Because the significance is <0.05, the H2 hypothesis is accepted. Based on the table with path analysis, the effect of interest rates on profitability with a T-statistic value of 0.088 and above the significance value <0.05 with a value obtained of 0.930, the H3 hypothesis is not accepted. Interest rates do not significantly affect the level of profitability obtained by the company.

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Based on the table with path analysis, the effect of interest rates on company profits with a T-statistic value of $2.328 > 1.96$. Because the significance is < 0.05 , the H4 hypothesis is accepted. Based on the table with path analysis, it can be seen that the influence of the Profitability Level on company profits shows a T-statistic value of 0.493 where the P Value is 0.626 or above the significance value of < 0.05 , so hypothesis H5 is not accepted. there is no significant influence between the level of profitability on company profits, there are many factors that support the increase/decrease in profits generated by the company, both internal and external factors.

DISCUSSION

Influence of Non-Performing Loans (X1) Towards Profitability (Z)

The result of the study show that non-performing loans affect profitability as measured by Return On Assets (ROA), which shows that the greater the NPL value obtained by a company, will have significant effect on the ups and downs of the profit earned. This is reinforced by research (Kaaya & Pastory, 2013) which states that lending is one of the main income for banking, therefore a large credit portfolio increases bank profitability.

Influence of Non-Performing Loans (X1) Towards Profits (Y)

The result of the study show that non-performing loans affects profits, which shows that the greater the NPL value obtained by a company, the higher the level of probability it will significantly influence. This is supported by research from (Kithinji, 2010) that healthy credit policies will help improve the monitoring of asset quality or income.

Influence of Interest Rates (X2) Towards Profitability (Z)

From the results of this study, it can be concluded that interest rates do not significantly influence the company's profitability. This statement is supported by research from (Crowley, 2007) that stated the influence of changing interest rates directly related to inflation, not on the profitability obtained.

Influence of Interest Rates (X2) Towards Profit (Y)

The results of the study show that interest rates have an influence on profits, which shows that the rise and fall of the interest rate set will affect the profits earned by the company, this is due to the size of the debtor's interest in the service products offered. This was also concluded by previous researchers who stated that

Influence of Profitability (Z) Towards Profit (Y)

From the results of the study, it can be concluded that Profitability, as measured by Return on Assets, does not significantly influence the profit earned by the company. This is supported by the many other factors (internal and external) that affect the company's profit. This was also concluded by previous researchers who stated that high NPL reduces cost efficiency and affects the increase/decrease of NPL and profitability. This reinforces that the increase/decrease in profit is influenced by many factors, one of which is the cost factor. (Sazzad et al., 2019)

IMPLICATIONS

This research can provide implications for companies in the banking sector. The results of the research can assist company management in making decisions about company performance in the future. Based on the research results, it is known that the non-performing loan variable has a significant effect on company profits. In this regard, it is necessary to make efforts for the management of banking companies in managing non-

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performing loans. From these results, it is also known that interest rates do not significantly influence the level of profitability.

CONCLUSION

In this study, three hypotheses were accepted, namely H1, H2, and H4. Two hypotheses that are rejected are H3 and H5. From the results of the tests, there was no significant effect between bank interest rates on the level of profitability and no significant effect between the level of profitability on profits generated by the company according to the sample financial statements of PT. BPR Duta Adiarta Medan. The main point in this research is risk control and non-performing loan analysis is an important thing that is continuously improved because it greatly affects the profit generated. From data obtained, it also shows that controlling non-performing loans from 2015 to 2022 has increased the company's profits. In addition to the company's policy regarding interest rate provisions, which are set regardless of monetary policy and the inflation rate, it greatly influences customer decisions, which affects the profitability value obtained. The existence of a relationship between one variable and another variable shows a significant relationship. In addition for future research, bigger respondents and varied variables and indicators will be better.

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