

WHICH SUBSIDIARIES CONTRIBUTE TO TELKOM GROUP VALUE OF THE FIRM (Case Study EVA Approach to Telkom Group from 2009 to 2014)

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Abstract

This research is conducted to show how positive the contribution of each subsidiary to Telkom Group and to see how the performance of both PT Telkom and the subsidiaries are by using EVA. The subsidiaries included in the research are PT Telkomsel, PT Dayamitra Telekomunikasi (Dayamitra), PT Multimedia Nusantara (Metra), and PT Telekomunikasi Indonesia Internasional (TII/Telin). The method used in this research is Spearman rank correlation coefficient. All of the EVA values can be found by collecting financial statements of the five companies mentioned above from 2009 to 2014. After the EVA values are found, each subsidiary's EVA values are compared to Telkom Group's EVA values and being ranked using Spearman rank. From the rank, it can be shown the contribution of each subsidiary to Telkom Group. According to the research result, there is only one subsidiary that has always positive EVA values and gives positive contribution towards Telkom Group, which is PT Telkomsel. The other subsidiaries are all have negative EVA values and show negative contribution towards Telkom Group. It is recommended for PT Telkom as the parent company to evaluate the subsidiaries that have negative EVA values.

Keywords: Contribution, Economic Value Added, Negative, Performance, Positive, Spearman rank, Subsidiary, Telkom Group.

1. Introduction

Telkom Group is the only state-owned telecommunications enterprise as well as telecommunications and network service providers in Indonesia. Telkom Group serves millions of customers throughout Indonesia with a complete range of telecommunications services that includes fixed wireline and fixed wireless connections, mobile communications, networking and interconnection services and Internet and data communication services. Telkom Group also provides various services in the field of information, media and edutainment, including cloud-based and server-based managed services, e-Payment services and IT enabler, e-Commerce and other portal services. In order to increase business value, in 2012, Telkom Group changed its business portfolio into TIMES (Telecommunication, Information, Media & Edutainment Service). To run its business portfolio, Telkom Group has four subsidiaries, namely PT. Telekomunikasi Indonesia Selular (Telkomsel), PT. Telekomunikasi Indonesia International (Telin), PT. Telkom Metra dan PT. Daya Mitra Telekomunikasi (Mitratel).

The goal of all companies is to create value for the shareholder. Telkom Group uses financial ratios to show how profitable the company is. The ratio that is used to show the percentage of how profitable a company's assets are in generating revenue is called ROA (return of assets). Return on assets gives an indication of the capital intensity of the company. Another ratio is ROE (return of equity). It is a ratio to measures the rate of return for ownership interest (shareholders' equity) of common stock owners. It measures the efficiency of a firm at generating profits from each unit of shareholder equity, also known as net assets or assets minus liabilities. ROE shows how well a company uses investments to generate earnings growth.

However, despite companies use financial ratios to simplify their financial statements, ratios also have limitation, such as: (1) Different companies operate in different industries each having different environmental conditions such as regulation, market structure, etc. Such factors are so significant that a comparison of two companies from different industries might be misleading; (2) Financial accounting information is affected by estimates and assumptions. Accounting standards allow different accounting policies, which impairs comparability and hence ratio

analysis is less useful in such situations, and (3) Ratio analysis explains relationships between past information while users are more concerned about current and future information.

Based on the limitation from financial ratios usage, the criteria related to determine companies value and managers performance can be divided into two categories: (i) Traditional financial performance measures (Accounting measures), and (ii) Value based financial performance measures (Economic measures).

Several researchers and practitioners, notably Stern Stewart Consulting Company and Associates, have claimed that economic value added (EVA) is superior to traditional accounting measures in driving shareholder value. In 1989, a formula called EVA (Economic Value Added) was invented by Stern Stewart & Co., a global consulting firm. As developed by Stern Stewart & Co., EVA is calculated as a company's "net operating profit after taxes" (NOPAT) minus a dollar cost for the equity capital employed by the company. The dollar cost of equity capital employed by a company is equal to the company's equity capital (reported on its balance sheet) multiplied by a percentage return that the company's shareholders require on their investment. Expressed as a formula:

$$\text{EVA} = \text{"Net Operating Profit After Taxes"} - (\text{Equity Capital} \times \% \text{ Cost of Equity Capital}).$$

The outcome for EVA is a measure of the contribution of the firm's operations for the period to the value of firm.

Based on the Vision, Mission, Strategic Initiatives, the amount of subsidiaries that are owned by PT Telkom, and the financial highlights amount that keep growing year by year, the writer analyzes the profitability of Telkom Group subsidiaries that will be measured by EVA with the research titled: **Which Subsidiaries Contribute to Telkom Group Value of the Firm (Case Study EVA Approach to Telkom Group from 2009 to 2014).**

Problem Identification

From the background research elaboration, the problems can be identified: How positive the contribution of each subsidiary to Telkom Group Value of the Firm is.

Research Objectives

To find out how positive the contribution of each subsidiary to Telkom Group Value of the Firm is.

2. Theoretical Review, Theoretical Framework and Hypothesis

The Goal of the Company/Firm

According to Keown *et al.* (2005:4): Goal of the firm should be maximization of shareholder wealth, by which we mean maximization of the price of the existing common stock. Not only will this goal be in the best interest of the shareholders, but it will also provide the most benefits to society. It is supported by Hill (2009:420) stating that "A firm's strategy can be defined as the actions that managers take to attain the goal of the firm. For most firms, the preeminent goal is to maximize the value of the firm for its owners, its shareholders." So the goal of the company/firm is to maximize or to continually increase shareholder value in the long-run, which is reflected by the price of the existing common stock. In other words, the goal of the company/firm is long-run survival. The goals of the company/firm are the targets, or end results, toward which it directs its energies. A firm's managers serve as agents for owners in striving to increase its value, a principal goal of all businesses.

The Value of the Firm

"Value of the firm is the price for which the firm can be sold, which equals the present value of future profits." (Maurice, Thomas, 2002; in Rustendi and Jimmi: 415).

According to Van Horne (1998:3-4) "The objective of a company must be to create value for its shareholders. Value is represented by the market price of the company's common stock, which in turn is a function of the firm's investment, financing, and dividend decisions. The market price of a firm's stock represents the value that market participants place on the company."

So the value of the firm is represented by market price of the company's common stock that reflecting the market value of a whole business. The value of the firm is the present value of the firm's current and future profits. The value of a firm is linked to profit maximization. A firm looking to maximize their profits is actually concerned with maximizing its value.

To maximizing its value for shareholders, it is needed the actions that managers take to increase the value of the firm to the shareholders by using three major decisions: the investment decision, the financing decision, and the dividend decision. Each must be considered in relation to our objective, an optimal combination of the three will create value.

Economic Value Added (EVA)

According to Keown *et al* (2005:445), if the manager must evaluate the performance of the firm over specific intervals of time – say one year. For this purpose, we calculate the firm's economic value added, or EVA.

$$\text{EVA} = (\text{net operating profit after tax (NOPAT)}) - (\text{weighted average cost of capital} \times \text{invested capital})$$

Where:

$$\text{NOPAT} = \text{Earning After Tax (EAT)} + [(\text{Interest/Finance Cost}) \times (1 - \text{Tax})]$$

$$\text{Weighted average cost of capital} = (\text{after tax cost of debt} \times \text{proportion of debt financing}) + (\text{cost of equity} \times \text{proportion of equity financing})$$

$$\text{Invested Capital} = \text{Long-term Debt} + \text{Equity}$$

From EVA calculation, the results will be interpreted as following:

- a. $\text{EVA} > 0$, a positive EVA reflects that the company increases its value to its shareholders. In this case, employees have the right to get bonus, creditors keep getting the interest, and shareholders can get the same or more return than what the shareholders invest.
- b. $\text{EVA} = 0$, it means breakeven, since all of the profits are used to pay the creditors and shareholders. Employees will not get bonus at this point.
- c. $\text{EVA} < 0$, reflects that the company does not give any added value or diminishing its value to the shareholders because the available fund cannot fulfill the expectation of creditors and shareholders. Employees will not get the bonus and shareholders will not get the return more than what they have invested.

All of Telkom subsidiaries are closed companies. Because of that, there will be assumptions in using WACC formulas to count the EVA total for Telkom subsidiaries: 10.50% cost of debt (corporate credit for prime lending rate of state-owned bank: Bank Mandiri) and 21% cost of equity (the average of IHSG /year).

Theoretical Framework

A company or a firm can be a private or public company. For public company, stock is widely held and available for sale to the public. A company or a firm can do corporate expansion; one of it is share exchange or stock acquisition. In stock acquisition, a controlling interest (typically, more than 50%) of another company's voting, common stock is acquired. The company making the acquisition is termed the parent, and the company acquired is termed a subsidiary. The parent can own more than one subsidiary. A parent and all its subsidiaries together are called a "group". The parent and its subsidiaries create their own financial statements, although, for external financial reporting purposes, the company will combine their individual financial statements into a single set of consolidated statements is named consolidated financial statement.

The goal of the company/firm is to maximize or to increase shareholder value in the long run. It means maximization of the price of the existing common stock. The market price of a firm's stock represents the value that market participants place on the company. So the value of the firm reflecting the market value of a whole business, include the parent and its subsidiaries.

The performance of the company, in this context “group”, can be seen and measured through consolidated financial statements, so the company performance is a reflection from all of the existing subsidiaries performance.

Company financial performance can be measured by using economic value added (EVA). So, with economic value added (EVA) can be analyzed and known how many subsidiary that contribute to Telkom Group Value of the Firm is and how significant the contribution of each subsidiary contribute to Telkom group value of the firm.

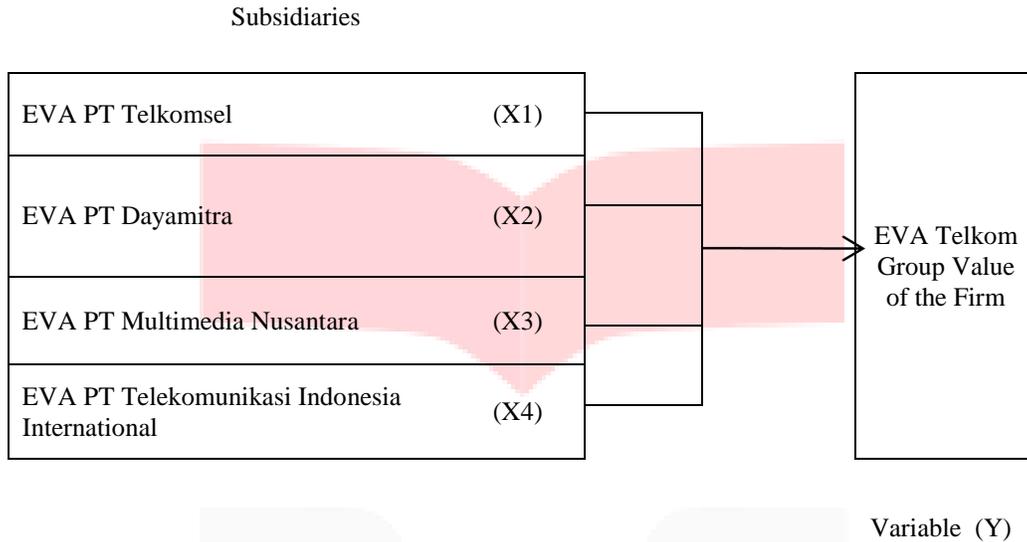


Figure 1. Theoretical Framework

Research Hypothesis

Based on theoretical framework above, so the formulation of research hypothesis is: *there is positive contribution from subsidiary to Telkom Group value of the firm.*

3. Research Methodology

Type of Research

This research will be conducting hypothesis testing with descriptive method. Hypothesis testing research is testing that explain temporary phenomenon or statement from the relation between two or more variables. Hypothesis research is developed based on existing theories and then tested based on collected data.

Operational Variable

The X variables are the EVA from each subsidiary, which are EVA PT Telkomsel (X1), EVA PT Dayamitra (X2), EVA PT Multimedia Nusantara (X3), and EVA PT Telekomunikasi Indonesia International (X4), while the Y variable is the EVA from Telkom Group. The indicator that is used to measure financial performance from each subsidiary and Telkom Group is Economic Value Added (EVA) approach. This research uses ratio scale both for X and Y variables.

Population and Sample

The population in this research is PT Telkom as a group (consolidation) and its subsidiaries from 2009 to 2014, while the sample in this research is taken with purposive sampling methodology with following criteria:

1. PT Telkom as a group (consolidation), which is PT Telkom as a go public state-owned company listed on the Indonesia Stock Exchange (IDX) and the New York Stock Exchange (NYSE).
2. Subsidiaries of PT Telkom which have existed since 2009 and still operate until the year 2014.
3. This research will focus only for the big four of Telkom subsidiaries.

Data Collection

The author gathers quantitative data for this research. Data collected in this research is a secondary data. The data is collected from PT Telkom consolidated financial statements and the subsidiaries financial statement. Data collection technique that is used in this research is study literature, a study that is done by studying various written sources and documents such as financial statements, journals, and other sources which are related with research topic.

Data Analysis Technique

The Spearman Rank Correlation Coefficient

Data analysis technique that is used in this research is Spearman rank correlation coefficient. Spearman rank correlation coefficient is a non-parametric test that is used to measure the degree of association between two variables. The following formula is used to calculate the Spearman rank correlation coefficient:

$$r_s = 1 - \frac{6 \sum d_i^2}{n(n^2-1)}$$

Where:

$d_i = x_i - y_i$ are the differences in the rank of x_i and y_i

n = the number of sample size

The Spearman correlation coefficient satisfies the usual requirements of correlation measures. It is equal to 1 when the variables X and Y are perfectly positively related, that is, when Y increases whenever X does, vice versa. It is equal to -1 in the opposite situation, where X increases whenever Y decreases. It is equal to 0 when there is no relation between X and Y. Values between these extremes give a relative indication of the degree of association between X and Y.

To identify whether or not the relationship of two variables are strong, Cohen (1988), Davis (1971) and De Vaus (2002); in Kemp: 96 provide useful orientation by suggesting comparable descriptors of various sized correlation coefficients.

Table 1 Table of Interpretation Correlation Coefficient

Correlation Coefficient	The Strength of The Relationship
0.00	No Correlation (No Relationship)
0.01 – 0.09	Trivial Relationship
0.10 – 0.29	Low Relationship
0.30 – 0.49	Moderate Relationship
0.50 – 0.69	Strong Relationship
0.70 – 0.90	Very Strong Relationship
≥ 0.90	Near Perfect Relationship

4. Research Results and Discussion

Research Results

This chapter will reveal the EVA values of Telkom Group and each Telkom subsidiary that are included in this research: EVA PT Telkomsel, EVA PT Dayamitra, EVA PT Multimedia Nusantara (Metra) and EVA PT Telekomunikasi Indonesia International (TII). After that, EVA from the subsidiaries (X1 - X4) will be analyzed whether they give contribution to Telkom Group (Y) or not by using Spearman rank correlation coefficient. The subsidiaries that give any contribution to Telkom Group will be identified from the analysis. EVA from Telkom Group and the subsidiaries are summarized in this table:

**Table 2 EVA PT Telekomunikasi Indonesia Tbk and Its Subsidiaries
(in billions of rupiah)**

No	EVA	Years Ended December 31,					
		2009	2010	2011	2012	2013	2014
1	PT Telekomunikasi Indonesia (Group)	7,851.17	7,542.76	7,720.02	9,298.68	8,289.52	8,257.96
2	PT Telekomunikasi Selular	6,540.62	5,124.89	4,823.10	6,393.88	7,168.05	8,525.45
3	PT Dayamitra Telekomunikasi	(95.03)	(64.92)	(23.11)	(48.45)	(92.91)	(271.12)
4	PT Multimedia Nusantara	(258.64)	(356.93)	(249.86)	(333.24)	(537.56)	(436.49)
5	PT Telekomunikasi Indonesia International	(171.42)	(86.64)	(16.72)	(168.80)	(100.12)	(459.49)

After knowing the results of each EVA value from Telkom Group and the subsidiaries, the table above is the summary of EVA. Telkom Group and Telkomsel have positive EVA, while the other: PT Dayamitra, PT Metra and PT TII have not really good EVA values.

The table below shows the analysis testing result by using Spearman rank correlation coefficient for all Telkom's subsidiaries.

Table 3 Analysis Testing Result

No	Subsidiaries	Analysis Result	Interpretation Correlation Coefficients	
		rs	Correlation Coefficients	The Strength of the Relationship
1	PT Telekomunikasi Selular	0.543	between 0.50 and 0.69	strong
2	PT Dayamitra Telekomunikasi	(0.143)	between -0.10 and -0.29	low negative
3	PT Multimedia Nusantara	(0.371)	between -0.30 and -0.49	moderate negative
4	PT Telekomunikasi Indonesia International	(0.486)	between -0.30 and -0.49	moderate negative

The table below showed the hypothesis testing result by using Spearman rank correlation coefficient for all Telkom's subsidiaries.

Table 4 Hypothesis Testing Result

No	Subsidiaries	Hypothesis Testing Result				
		Sig	α	Sig > or < from α	Accept or Reject H0	Contribution
1	PT Telekomunikasi Selular	0.133	0.05	>	accept H0	Negative
2	PT Dayamitra Telekomunikasi	0.394	0.05	>	accept H0	Negative
3	PT Multimedia Nusantara	0.234	0.05	>	accept H0	Negative
4	PT Telekomunikasi Indonesia International	0.164	0.05	>	accept H0	Negative

Discussion

This research uses four variables as the X variables which are: EVA PT Telkomsel (X1), EVA PT Dayamitra (X2), EVA PT Metra (X3) and EVA PT TII (X4), and one variable as the Y variable which is EVA Telkom Group. The results of EVA calculations towards Telkom Group and its subsidiaries show that the companies that has EVA > 0 or positive EVA annually are Telkom Group and PT Telkomsel, while the companies that has EVA < 0 or negative EVA annually are PT Dayamitra, PT Metra, and PT TII.

After the value of EVA of Telkom Group and the subsidiaries are obtained, the next step is to identify the contribution towards Telkom Group value of the firm and how positive the contribution of each subsidiary to Telkom Group value of the firm is using Spearman rank correlation coefficient and data processing using SPSS version 22. The results, as shown in the analysis testing result table above, for PT Telkomsel, the coefficient correlation is .543. It means that there is a positive relationship. The coefficient correlation for PT Dayamitra Telekomunikasi is (.143). It means that there is a negative relationship. The coefficient correlation for PT Metra is (.371). It means that there is a negative relationship. The coefficient correlation for PT TII is (.486). It means that there is a negative relationship.

Each correlation coefficient of the subsidiaries and the strength of the relationship are identified by using SPSS version 22. The significant value for PT Telkomsel is .133 which is higher than 0.05 (α), it means accept H0: there is negative contribution from Telkomsel to Telkom Group value of the firm. The significant value for PT Dayamitra is .394 which is higher than 0.05, it means accept H0: there is negative contribution from PT Dayamitra to Telkom Group value of the firm. The significant value for PT Metra is .234 which is higher than 0.05, it means accept H0: there is negative contribution from PT Metra to Telkom Group value of the firm. The significant value for PT TII is .164 which is higher than 0.05, it means accept H0: there is negative contribution from PT TII to Telkom Group value of the firm. However, it should be noted that there are some reasons on why PT Telkomsel gives Telkom Group negative contribution, which are because NOPAT data of Telkom Group in 2012 increased sharply. In 2012, there was proceed from insurance claims of Telkom-3 satellite that failed to reach its orbit amounting to Rp1,772 billion recorded as part of other income. Since the income is included in the parent company's financial report, it makes Telkomsel give quite small contribution, while actually Telkomsel contributes to Telkom Group the most. From the analysis above, it can be identified that the only subsidiary that give contribution to Telkom Group Value of the Firm is PT Telkomsel with correlation coefficient .543, which means PT Telkomsel has strong relationship. The other three subsidiaries, which are PT Dayamitra, PT Metra and PT TII, give negative contribution to Telkom Group Value of the Firm because all of the correlation coefficients are negative.

5. Conclusions and Suggestions

Conclusions

According to the results of descriptive analysis by using EVA approach, Spearman rank correlation coefficient analysis, and hypothesis test that has been done in the previous chapter, some conclusions can be drawn:

1. EVA values of PT Telkomsel are always positive every year, so there is positive contribution from PT Telkomsel to Telkom Group Value of the Firm. The relationship between PT Telkomsel and Telkom Group is strong: 0.543.
2. There is negative contribution from PT Dayamitra to Telkom Group Value of the Firm, where the relationship between PT Dayamitra and Telkom Group is low negative: (0.143).
3. There is negative contribution from PT Metra (Multimedia Nusantara) to Telkom Group Value of the Firm, where the relationship between PT Metra and Telkom Group is moderate negative (0.371).
4. There is negative contribution from PT TII (Telekomunikasi Indonesia International) to Telkom Group Value of the Firm, where the relationship between PT TII and Telkom Group is moderate negative (0.486).
5. All subsidiaries have negative contribution towards Telkom Group value of the firm, except PT Telkomsel. While this seems to be the case, there are actually reasons on PT Telkomsel seems to not contribute much to Telkom Group.

Suggestions

1. For the Company

Based on the conclusions found in this research, therefore some suggestions are proposed to Telkom Group:

- 1) PT Telkom as the parent company is recommended to evaluate the subsidiaries that have negative EVA, because if the subsidiaries keep having negative EVA, even tend to have negative EVA every year progressively, it will impact the performance of Telkom Group for years to come.
- 2) PT Telkom should not be satisfied with positive EVA. Because PT Telkom only depends on PT Telkomsel which is the only subsidiary that has positive EVA and give positive contribution to Telkom Group. PT Telkom should be able to find solution to increase its own performance and the subsidiaries performance (other than PT Telkomsel).

2. For Further Researchers

This research use data of six years for finding EVA values which is from 2009 until 2014. It is possible for further researchers to research, analyze and test whether the results of Telkom Group subsidiaries EVA is getting better in the upcoming years.

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