Advances in Business, Management and Entrepreneurship

ADVANCES IN BUSINESS, MANAGEMENT AND ENTREPRENEURSHIP

Edited by

Ratih Hurriyati, Benny Tjahjono, Ikuro Yamamoto,
Agus Rahayu, Ade Gafar Abdullah
and Ari Arifin Danuwijaya

CRC Press
Taylor & Francis Group

Advances in Business, Management and Entrepreneurship

ISSN 2639-8249
(Online) ISSN 2639-8257

Book series editor

Ratih Hurriyati
Universitas Pendidikan Indonesia, Bandung, Indonesia

PROCEEDINGS OF 3RD GLOBAL CONFERENCE ON BUSINESS MANAGEMENT AND ENTREPRENEURSHIP (GC-BME 3), BANDUNG, INDONESIA, 8 AUGUST 2018

Advances in Business, Management and Entrepreneurship

Editors

Ratih Hurriyati

Universitas Pendidikan Indonesia, Indonesia

Benny Tjahjono

Coventry University, Indonesia

Ikuro Yamamoto

Kinjo Gakuin University, Japan

Agus Rahayu, Ade Gafar Abdullah & Ari Arifin Danuwijaya

Universitas Pendidikan Indonesia, Indonesia

CRC Press
Taylor & Francis Group
Boca Raton London New York

CRC Press is an imprint of the
Taylor & Francis Group, an **informa** business
A BALKEMA BOOK

0808
2018 GCbMe
Global Conference on Business, Management, and Enterpreneurship

CRC Press/Balkema is an imprint of the Taylor & Francis Group, an informa business

Typeset by Integra Software Services Pvt. Ltd., Pondicherry, India

Library of Congress Cataloging-in-Publication Data

Applied for

Published by: CRC Press/Balkema
Schipholweg 107C, 2316XC Leiden, The Netherlands e-mail: Pub.NL@taylorandfrancis.com
www.crcpress.com – www.taylorandfrancis.com

ISBN: 978-0-367-27176-3 (Hbk)
ISBN: 978-0-429-29534-8 (eBook)
DOI: https://doi.org/10.1201/10.1201/9780429295348

Advances in Business, Management and Entrepreneurship – Hurriyati et al (eds)
© 2020 Taylor & Francis Group, London, ISBN 978-0-367-27176-3

Table of Contents

Advances in Business, Management and Entrepreneurship – Hurriyati et al (eds)
© 2020 Taylor & Francis Group, London, ISBN 978-0-367-27176-3

Analysis of return on equity, current ratio and debt to equity ratio on Islamic stock price Jakarta Islamic Index

M. Masrizal, T. Widiastuti, I. Mawardi & W. Wisudanto
Universitas Airlangga, Surabaya, Indonesia

ABSTRACT: Before deciding to invest in certain stocks, investors are faced with a desire to get maximum return. One of the basic indicators for the assessment is financial performance. This study aimed to analyze of return on equity, current ratio and debt to equity ratio on Islamic stock prices listed in Jakarta Islamic Index (JII). The research used quantitative approach with regression analysis using panel data in EViews. As for sampling, purposive sampling method produced sample of 8 companies listed as consistent issuers recorded in JII from 2009 to 2017. The empirical results showed that independent variables of return on equity, current ratio and debt equity ratio simultaneously had a significant influence on stock prices. Partially, ROE and DER were the only variables that had a significant effect on stock prices, while current ratio had no significant influence on stock prices. The results of this study served as a basis for decision making for investors.

1 INTRODUCTION

The stock market is an important channel for the corporate sector to raise capital needed for invest-ment and business activities (Shin & Thaker 2017). Stock markets perform a key function in providing the necessary critical links between companies that need funds to start new businesses or to expand their current operations and investors who have surplus funds to invest in such companies (Avdalovic & Milenkovic 2017).

The stock price index is an indicator showing the movement of stock prices. Stock index serves as an indicator of market trends. In other word, the movement of the index describes market conditions ata time, whether the market is active on trading or vice versa. One of the most attractive sectors to in- vest in Indonesia's capital market is the shares that belong to the Jakarta Islamic index (JII) group. This can be seen from the capitalization of Jakarta IslamicIndex, which has an increasing trend for the last 6 years.

The companies listed in the JII conduct their business activities in compliance with Islamic principles. The Jakarta Islamic Index is an index of 30 stocks of companies that put in their investments in Islamic way. JII is a sharia-based index (Hadi 2015).

A study conducted by Wardhana et al. (2011) discovered that although the sharia capital market is affected by changes in market prices during financial crises in the United States, impacts are more severe in conventional capital markets. The sharia capital market has proved to have a better ability to adapt to external changes and disruptions. Thus, it can be concluded that the sharia capital market has more resistance to crises than conventional capital markets.

Before deciding to invest in certain stocks, investors have a desire to get maximum returns. In addition, investors are exposed to the risks associated with the investments. The most common way to assess stock prices is through a fundamental analysis of the company.

According to Darmadji and Fakhruddin (2012), fundamental analysis is a way to conduct stock valuation by studying or observing various indicators related to macroeconomic and industry conditions of a company as well as various financial indicators and understanding the company management.

To assess company performance and evaluate its value, some commonly used indicators, including profit margins and other financial data, are used. A prospective investor assesses company performance gradually. One of the basic indicators for assessment is net income/profit. The higher the net profit, the higher the stock price in the market, which leads to increased demand (Utari et al. 2014). Profitability is the ability of management to earn a profit. One of the profitability analyses is return on equity ratio (ROE).

Liquidity is the ability of the company to meet all of its obligations according to their maturity. Liquidity is realized if the level of current assets is greater than the current debt or liability. One of the liquidity ratios is the current ratio (CR), defined as the ratio that compares the current assets of the company with short-term debt (Sutrisno 2017).

Leverage is the company's ability to use debt to finance investment. The ideal ratio of total debt to asset is 40%. However, in good economic conditions, leverage can be high, as the business is expected to generate higher operating profit (Utari et al. 2014). The level of corporate risk is reflectedinthe ratio of debt to equity (DER). This shows the ability owned by the company to pay off its obligations.

Based on previous research and the phenomenon described earlier, the authors conducted research to analyze the influence of Return on Equity (ROE), Current Ratio (CR) and Debt to Equity Ratio (DER) on share prices in the Jakarta Islamic Index (JII) between 2009 and 2016.

1.1 Return on equity

Return on Equity (ROE) is the indicator used toassess the effectiveness of investments by capitalowners and to consider whether to maintain that in- vestment in a competitive system. A high rate of re- turn on capital incites for investment and facilitates reinvestment of profits as a source of future growth of the company, to the detriment of its immediate distribution as dividends. Return on equity expressesequity ability to create added value, after remuner- ation of borrowed capital, which will allow share- holders equity compensation and self-financing of the company (Vasiu 2016).

ROE is the ratio between profit after tax and equity. This is a measurement of the income avail- able to the owner of the company for the capital invested in the company (Widayanti et al. 2009). Theratio gives a clue of company's ability to gener- ate profits with its owned capital. This ratio shows the efficiency of capital utilization. Higher ROE indicates better company's performance. The share- holders received higher return and vice versa (Kasmir 2015).In other words, higher ROE indicateshigher profits gained by the shareholders. The investor will favor this performance so that the stock price will rise (Takarini & Hendrarini 2011). Studiesconducted by Shin and Thaker (2017) and Al- Omoush and Al- Shubiri (2013) stated that return on equity (ROE) provides a significant positive relation-ship to stock prices, supporting this statement.

1.2 Current ratio

The current ratio shows company liquidity as meas- ured by comparing current assets to current debt (Keown et al. 2011). A high current ratio (CR) increase investors' confidences to invest their capital to the company. According to Sutrisno (2017), cur- rent ratio is a financial ratio that compares current assets owned by a company with short-term debt. Current assets include cash, trade receivables, secur- ities and inventories. While short-term debt includes trade payables, notes payable, bank loans, payables and other debts that must be paid immediately. Thus, it can be said that a high current ratio indicates that a company is able to fulfill its obligations or short- term debt by using current assets. In addition, high current ratio increases the confidence of shareholders to the company for paying its obligations.

This statement is supported by research conduct- ed by Kohansal et al. (2013) and Banchuenvijit (2016), which states that current ratio has a significant influence on stock prices.

1.3 Debt to equity ratio

Debt to Equity Ratio (DER) is one leverage ratio or solvency. Solvency ratio is the ratio to determine the company's ability to pay obligations if the company is liquidated.

According to Kasmir (2015), debt to equity ratio is a ratio that is used to assess debt with equity. Investors want to invest in companies with a debt equity ratio that does not exceed the debt limit and is no more than the company's capital. Debt ratio reflects the level of a company's risk, investors are notonly in favor of profit, but also concerned with the level of risk exposed to the company. Investors should avoid investing in companies with high debt- to- equity ratios as they reflect a higher level of risk. This statement is supported by research conductedby Suparningsih (2017), Nordiana and Budiyanto (2017), Rahmawati and Suryono (2017), and Vedd and Yassinski (2015), which stated that the debt equity ratio (DER) has a significant effect on stock prices.

2 METHOD

This study is a quantitative research and conducted by collecting data in the form of price data obtained from Bursa Efek Indonesia (Indonesia Stock Exchange) and financial reports obtained from the official company website. The sampling technique used for the study was purposive sam- pling technique, which could be understood as sample determination technique with certain con- sideration (Sugiyono 2015). The result of sampling produced eight companies that were consistently recorded in the Jakarta Islamic index: Astra Agro Lestari Tbk, Astra Internasional Tbk, IndocementTunggal Perkasa Tbk, Kalbe Farma Tbk, LondonSumatra Indonesia Tbk, Semen Indonesia Tbk, Tel- ekomunikasi Indonesia Tbk and Unilever Indonesia Tbk. Regression analysis of panel data was used for the data analyses. Such data could be obtainedby observing a series of cross section observations over a given period (Ariefianto 2012). According to Manurung et al. (2010), a regression model of panel data can be done using three approaches: Common Effect or Pooled Least Square (PLS) method, Fixed Effect Model (FEM) method and Random Effect Model (REM) Method. The ana- lysis was conducted using EViews 9 computer software.

3 RESULT AND DISCUSSION

Table 1 shows the multiple regression results using panel data.

Table 1. Panel data regression results.

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-2917.137	2680.010	-1.088480	0.2807
ROE	188.4983	69.75906	2.702134	0.0089
CR	2.462611	7.578880	0.324931	0.7463
DER	117.6446	31.77425	3.702514	0.0005
Cross-section fixed (dummy variables)				
R-squared	0.878607	Mean dependent var		11,568.54
Adjusted R-squared	0.858706	S.D. dependent var		10,993.32
S.E. of regression	4132.290	Akaike info criterion		19.63081
Sum squared resid	1.04E+09	Schwarz criterion		19.97864
Log likelihood	-695.7093	Hannan-Quinn criter.		19.76928
F-statistic	44.14987	Durbin-Watson stat		0.946759
Prob (F-statistic)	0.000000			

Based on the data in Table 2, the regression equation can be described as follows:

$$Y = 2917.137 + 188.4983X1 + 2.462611X2 + 117.6446X3 \quad (1)$$

where Y = share price; C = constanta; X1 = return on equity; X2 = current ratio; and X3 = debt to equity ratio.

The result of this equation gives the value of -2917.137 as a constanta value (a) indicating the absence of return on equity, the current ratio and debt to equity ratio, offer the value of stock price is -2917.137. Moreover, the value of regression coefficient of return on equity equals to 188.4983 explains, every one-unit increase for return on equity will rise the stock price to 188.4983. Furthermore, the value of 2.46261 is a regression coefficient that explains every one-unit increase for current ratio will be a rise in stock price to 2.46261. Additionally, 117.6446 isa regression coefficient that explains every one-unit increase for debt to equity will result the increase of value of stock price to 117.6446.

3.1 *Discussion*

Based on data processing that has been done showed, return on equity have significantly affected stock price. Profitability ratio measures the ability of a company to earn profits for its shareholders. Higher ROE indicates higher profits gained by the shareholders. The investor will favor this perform- ance so that the stock price will rise (Takarini & Hendrarini 2011). The results are in line with studiesconducted by Shin and Thaker (2017) and Al-Omoush & Al-Shubiri (2013) which stated that ROE provides a significant positive relationship to stock prices. However, the findings also show that current ratio has no significant effect on stock price. This contradicts the research findings from Kohansalet al. (2013) and Banchuenvijit (2016), which state that current ratio has a significant effect on stock prices.

Furthermore, the results showed that debt to equity ratio has significant effect on stock price. Thiscan be interpreted in this way: the use of company's debt will increase the company's revenue. The com- pany uses its leverage to finance its operating costs, with the aim that the profits earned by the company will be greater than the cost of assets and sources of funds, thereby increasing the profitability of share- holders. These findings are in line with results of studies conducted by Suparningsih (2017), Vedd andYassinski (2015), and Avdalovic and Milenkovic (2017), which state the debt equity ratio (DER) has a significant effect on stock prices.

The capital structure determines the earnings per share and the results of company owned capital. In good business conditions, using high leverage will accelerate the development of the company, for the reason that in general the operating profit is greater than the interest expense. Higher leverage contributes higher return on equity in good economic conditions (Utari et al. 2014). According to an OECD survey (OECD 2015), Indonesia's economic conditions show remarkable performance for a decade after the Asian crisis. Such performance is impressively generated from policy reforms implemented especially in terms of building robust macroeconomics frameworks.

This is also supported by the credit rating agency Standard & Poor's (S&P) that raised Indonesia's debt rating to a viable investment. The improved rating indicates Indonesia has the ability to be more resilientto external shocks as geopolitics issues. A number of macroeconomic policies issued are considered cap- able of maintaining economic stability. The inflation rate is under control, the rupiah exchange rate is rel- atively stable and the government is considered suc- cessful enough to maintain the supply of food.

4 CONCLUSION

The findings show that independent variables of return on equity, current ratio and debt equity ratio simultaneously have a significant influence on stock prices. Partially, ROE and DER are the only vari- ables that have a significant effect on stock prices, while current ratio has no significant influence on stock prices. Our recommendation is that investors should invest on shares that have high ROE andDER due to their significant effects on the return of index. Further research should look for other funda- mental factors that play important roles in determin- ing the stock price.

ACKNOWLEDGEMENT

We would like to extend a apreciation to the Faculty of Economic and Business Universitas Airlangga forgiving research funding for this topic.

REFERENCES

Al-Omoush, B.H. & AL-Shubiri, F.A. 2013. The impact of multiple approaches financial performance indicators on stocks prices: An empirical study in Jordan. *Journal of Global Business and Economics* 6(1): 1-11.

Ariefianto, M.D. 2012. *Ekonometrika esensi dan aplikasi dengan menggunakan eviews*. Jakarta: Erlangga.

Avdalovic, S.M. & Milenkovic, I. 2017. Impact of com- pany performances on the stock price: An empirical ana-lysis on select companies in Serbia. *Economics of Agriculture* 2: 561-570.

Banchuenvijit, W. 2016. Financial ratios and stock prices: Evidence from the agriculture firms listed on the stock exchange of Thailand. *UTCC International Journal of Business and Economics*.

Darmadji, T. & Fakhruddin, H.M. 2012. *Pasar modal di Indonesia: Pendekatan tanya jawab*. Jakarta: Salemba Empat.

Hadi, N. 2015. *Pasar modal*. Yogyakarta: Graha Ilmu.

Kasmir. 2015. *Analisis laporan keuangan*. Jakarta: Rajawali.

Keown, A.J., Martin, J.D., William, P.J. & Scott, D.F. 2011. *Manajemen keuangan* (10 ed). Jakarta: PT Indeks.

Kohansal, M.R., Dadrasmoghadam, A., Mahjori, K.K. &Mohseni, A. 2013. Relationship between financial ratios and stock price for the food industry firms in stock exchange of Iran. *World Applied Programming* 3(10): 512-521.

Manurung, J.J., Manurung, A.H. & Saragih, F.D. 2010. *Ekonometrika teori dan aplikasi*. Jakarta: PT Elex Media Komputindo.

Nordiana, A. & Budiyanto, B. 2017. Pengaruh DER, ROA dan ROE terhadap harga saham pada perusahaan food and beverage. *Jurnal Ilmu & Riset Manajemen* 6(2).

OECD. 2015. *Economic surveys Indonesia*.

Rahmawati, D. & Suryono, B. 2017. Pengaruh DPR, EPS dan DER terhadap harga saham. *Jurnal Ilmu dan Riset Akuntansi* 6(6).

Shin, W.K & Thaker, H.M.T. 2017. Macroeconomic varia-bles, financial ratios and property stock prices in Malaysia. *International Journal of Business and Innov-ation* 3 (1).

Sugiyono. 2015. *Statistik untuk penelitian*. Bandung: Alfabeta.

Suparningsih, B. 2017. Effect of debt to equity ratio (DER), price earnings ratio (PER), net profit margin (NPM), return on investment (ROI), earning per share(EPS) in influence exchange rates and Indonesian inter-est rates (SBI) share price in textile and garment indus-try Indonesia stock exchange. *International Journalof Multidiciplinary Research and Devlopment* 4(11): 58-62.

Sutrisno. 2017. *Manajemen keuangan teori: Konsep danap-likasi*. Yogyakarta: Ekonisi.

Takarini. N. & Hendrarini, H. 2011. Rasio keuangan dan pengaruhnya terhadap harga saham perusahaan yang ter-daftar di Jakarta Islamic Index. *Journal of Business and Banking* 1(2): 93-104.

Utari, D., Purwanti, A. & Prawironegoro, D. 2014. *Manaje-men keuangan*. Jakarta: Mitra Wicana Media.

Vasiu, D.E. 2016. Case study regarding the correlation between the main indicators of financial performance and the bet index, for the companies participating in the bet index. *Management and Economics*: 357-363.

Vedd, R. & Yassinski, N. 2015. The effect of financial ratios, firm size & operating cash flows on stock price: Evidence from the Latin America industrial sector. *Jour-nal of Business and Accounting* 8(1): 15-26.

Wardhana, W., Beik, I.S. & Setianto, R.H. 2011. Pasar modal syariah dan krisis keuangan global. *Iqtishodia Jurnal Ekonomi Islam Republika*.

Widayanti, R., Ekawati, H., Dorkas, A., Rita, M.R. & Sucahyo, U.S. 2009. *Manajemen Keuangan*. Salatiga: Fakultas Ekonomi UKSW