CHAPTER I

INTRODUCTION

1.1 Background

Indonesia has held 11 presidential elections with the first election held in 1955. However, people of Indonesia have chosen presidents and vice-presidents through direct election since 2004 with five candidates. The election was held in two rounds because none of the candidates got more than 50%. In the second direct presidential election in 2009, the election was held in one round with three candidates. The third direct election that was held in 2014 had only two candidates. Although there were only two candidates, there was still a fierce competition before and after the election. There were several black campaigns before the election that became hot issue in mass media. Nelson Simanjutak, the member of Bawaslu said that until June 27, 2014 there have been 34 reports of campaign infraction to Bawaslu such as the issue of Obor Rakyat, human right and other issues (www.jpnn.com).

After the election, the fierce competition reflected by the difference result from quick count. From 11 institutes that conducted a quick count, seven of them (Popili Center, CSIS, Litbang Kompas, Indikator Politik Indonesia, Lingkaran Survei Indonesia, Radio Republik Indonesia, and Saiful Mujani Research Center) showed that Joko Widodo- Jusuf Kalla as the winner, while the rest such as Puskaptis, Indonesia Research Center, Lembaga Survei Nasional, and Jaringan Suara Indonesia showed Prabowo Subianto-

Hatta Rajasa as the winner. The fierce competition attracted attention from many parties indicated by the participation from voters. In this presidential election, there were 193.944.150 voters, and 134.953.967 of them used their right to vote (www.detik.com). Chairman of KPU, Sigit Pamungkas on July 23, 2014 said that most voters have kept watching all of the election steps from list of voters, recapitulation, campaign, as well as debates compared with the previous presidential election although based on quantitative data the participant in this election was approximately 70%, a 2% decrease from the presidential election in 2009 (www.republika.com).

It is well known that political and economic condition have a close relationship. A lot of economic policies are influenced by politics like price policy of fuel, electricity, gas, tariff, and others. For example, several good (bad) political announcements could generate positive (negative) abnormal return in Nepal stock market that explained in research by Dangol (2007). Presidential election is one of the examples of political events. Based on researches in several countries, stock markets are influenced by election. In America, the stock market often hits major bottoms about two years before presidential elections and rises through the end of election years (Nickles, 2004). Nickles explained this was because of the executive branch of government influencing fiscal policy and past administrations have often used fiscal policy in a manner designed to pump up the economy just prior to a presidential election. These pre-election actions and campaign promises often have created some euphoria among voters and investors because economic stability followed by political stability will conduct feel of safety among investors to invest their fund and the expectation of investors to the new president reflected in price changing and volume of stock trading in stock market.

This phenomenon relates with the fundamental theory of market efficiency. In an efficient market, all available information will be embodied in stock price implying that investors cannot earn abnormal returns. In an election period, the rational investors will analyze voter sentiments from all available resources as their expectation. This makes the stock price move to reflect it.

Efficient market theory proven by what already happened in several countries not only in America but also in Taiwan, South Korea, Philippine, including Indonesia that had positive abnormal return in pre-election period. However, the same research revealed that the presidential election in Singapore didn’t have a significant effect to stock market because the ruling party in Singapore controlled the process of election, so the result of presidential election in Singapore was predictable. Based on Uncertain Information Hypothesis, the positive abnormal return in pre-election periods relates to uncertainty during that period and also affected by the level of political, economy, press freedom, and outcome of election (Liu, 2007). Another research shows that when the outcome of the election brings about a change in the political orientation of the government, it will increase the uncertainty, and the market tends to react in a more volatile manner (Bialkowski, 2006).

Research conducted by Liu during the Indonesian presidential election in 2004 had different result from the one conducted by Trisnawati (2014). It found through market model with OLS as the regression technique, there was no significant difference in average abnormal return and average trading volume activity in LQ-45 before and after presidential election in 2004. However there was different AAR before and after presidential election in 2009. Based on their analysis, no differences in AARR and ATVA showed that investors tend to wait and see in presidential election period to spend their fund for short term investments. In addition, quick count result at that time has a big possibility to win by incumbent that has a similar policy. While in 2014, the uncertainty was higher because there is no incumbent. So the economic condition in the future has bigger possibility to change and the electability polling of candidates before election always changes. Even after election there are significant differences between quick count and both candidates declared that they were the winner version quick count. Thus whether the higher level of uncertainties took place in the 2014 presidential election ensured the previous research or not about the influence of uncertainties in presidential election to the return and volume of stock trading.

The previous research used LQ-45 as the sample. While this research use the Kompas-100 index because it is considered reflects stock market due to the value of market capitalization around 70% from IHSG and the movement correlation was more than 95% (Viliawati, 2012). The other difference is the previous researches focused on the date around the date of the election, however this research focus on two important dates in presidential election when there is new information such as KPU announcement of the candidates and the winner of presidential election in 2014. Moreover, several researches relate election with uncertainty, so this research proves how big the uncertainty influence market reaction. The uncertainty represented by the date of the announcement of candidate because on that date, the investors still don't know who the next president is and more predictions about next policy rather than in the date of legal announcement of the winner of election.

So that is the reason why this research analyzes the return and trading volume around those dates to see whether there is market reaction or not in Kompas-100. It also compares market reaction between around the date of candidate announcement with result announcement. If there is immidiate market reaction means that the market semi-strong efficient market.

1.2 Problem Formulation

Based on the background above, the main problem in this research is to find whether there is a market reaction in Indonesia Stock Exchange (IDX) during the presidential election held in 2014. To know the answer of the main problem, the writer formulates research problems:

1. Is there any average abnormal return in index Kompas-100 around candidate announcement of the 2014 Indonesian presidential election?
2. Is there any cumulative abnormal return in index Kompas-100 around candidate announcement of the 2014 Indonesian presidential election?
3. Is there any average abnormal trading volume in index Kompas-100 listed in IDX around candidate announcement of the 2014 Indonesian presidential election?
4. Is there any average abnormal return in index Kompas-100 around result announcement of the 2014 Indonesian presidential election?
5. Is there any cumulative abnormal return in index Kompas-100 around result announcement of the 2014 Indonesian presidential election?
6. Is there any average abnormal trading volume in index Kompas-100 listed in IDX around result announcement of the 2014 Indonesian presidential election?
7. Is there any different market reaction around the announcement of the candidate and the announcement of the winner in the 2014 presidential election?

1.3 Contribution

1.3.1 Theory

This study aimed to test Efficient Market Hypothesis semi-strong form in IDX around the 2014 presidential election. Whether there is reaction as conclusion that the announcement has information content and it means the market is semi-strong form efficient market. While the previous research in many countries explain that the presidential elections contributing uncertainty condition can create abnormal return and give effect to volume trading, and in 2014, the uncertainty condition is higher, so the result of this research can ensure the previous research if this result shows that there will be significant differences compare to the previous election. The result of this research can also be an additional reference and comparability for future researches about EMH in Indonesian stock market.

1.4 Research Systematic

In order to investigate whether there were market reaction around the third direct presidential election in Indonesia it is a must to have an organize structure analysis. This study is developed in five chapters:

CHAPTER I : INTRODUCTION

This chapter explores the difference condition of the 2014 Indonesian presidential election until attracted attention indicated by participation of voter. This study aims to know whether there is market reaction or not in Kompas-100 index around the candidate announcement and result announcement. It compares reaction between around candidate and result announcement.

CHAPTER II : THEORETICAL REVIEW

This chapter explains about theory and some information which has the correlation to Efficient Market Hypothesis, event study, and market reaction toward published information especially political information. The previous research in general found market reaction around election in several countries. This chapter explained research hypothesis development and analytical framework.

CHAPTER III : RESEARCH METHODOLOGY

This chapter explained the research approach is quantitative with variable average abnormal return, cumulative abnormal return and average abnormal trading volume to measure market reaction. This chapter shows more about the operational definition and steps in hypothesis test.

CHAPTER IV : RESULT AND DISCUSSION

It contains the general description of research subject and object. It explained the result of hypothesis test based on the step explained in previous chapter. This chapter shows the summary of hypothesis test and the analysis.

CHAPTER V : CONCLUSION AND RECOMMENDATION

This chapter concludes from the research result and gives suggestion for the next similar research for better research development.