



## Effect of Profitability, Liquidity and Earning Management on Stock Return in IDX Companies

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### Abstract

This study aims to determine whether profitability, liquidity and earnings management can be used to predict the stock return of manufacturing companies listed in Indonesia Stock Exchange. Samples were obtained randomly on companies listed in Indonesia Stock Exchange as many as 100 companies with over 5-year study period from 2018 to 2022 year. The data used are secondary data from financial statements or annual reports from 2014 to 2018 year. The results showed that the profitability is partially a significant negative effect on Return Shares. Liquidity partially no significant effect on stock returns. Earnings management partially no significant effect on stock returns. and leverage no significant effect on stock returns. Profitability, liquidity, earnings management, and leverage simultaneously have a significant effect on stock returns.

**Keywords:** Profitability; liquidity; earnings management; leverage; .

### 1. Introduction

Along with the development of capital markets, the need for relevant information in investors' decision-making is also increasing. Capital market activities can not be separated from the availability of a wide range of information about the company or issuer. Such information would affect a wide range of decisions to be taken that result in changes in both price and quality of shares traded (Sangsoko and Shaliza, 2018). In general, investors will be interested in investing if the company can provide good stock returns (Siegel, 2021).

Information on stock returns is associated with information on the company's financial statements. Return is the difference of the amount received by the stakeholders and the amount invested by all the stakeholders (Cordeiro & Tewari, 2015). The return may be a return realization that has occurred or return expectations that have not occurred but is expected to occur in the future. According to Lasmet, Wiyono, and Murniati (2019), return realization and expectation can be calculated using the share price information in financial statements. If seen from a high rate of return, the company will give it to investors, showing that the performance of these companies can be said to be good (Nalurita, 2017).

Profitability provides an overview of a company's ability to generate profits at the rate of sales, assets, and certain share capital at a certain period (Fitriana, Andini, and Oemar, 2016), to assess the level of effectiveness of administration in running the company's operations. Profitability ratios can be measured by comparing the various elements of the income statement or balance sheet.

Agency theory was initially developed by Jensen and Meckling (1976), This theory explains the working relationship between the owners (principals) and management (agents). Principals party is the party giving the mandate to the other party, namely the agents to perform all activities on behalf of the owner of the company in his capacity as decision makers.

Stock return is owned by the profit rate of investors on a stock investment. Investors' interest is to increase the value of wealth by maximizing returns without forgetting the risk factors it faces (Edelen et al., 2016). High stock returns identifies that the stock is actively traded (Edelen et al., 2016).

Profitability shows the performance of the company in generating profits (Purba & Africa, 2019). If the company's financial performance in generating income increases, this would indicate an attraction for investors

or prospective investors to invest in the company. If the demand for shares increases, the share price will tend to rise. The higher profitability, the higher stock returns generated. From this it can be presumed that the profitability impact on stock returns (Sangsoko and Shaliza, 2018). Profitability ratios represented by Return on Assets (ROA) is the ability of the company makes a profit in relation to total sales of assets or equity. Based on research Oroh, Rate, and Kojo (2019) that the return on assets (ROA) affects stock returns.

*H<sub>1</sub>: Profitability has significant influence on stock return.*

Liquidity measures the company's ability to meet the company's current activity with current debt. If the liquidity generated by the higher a company, means the company is unable to pay obligations that have matured, it will affect the stock return. results of research using regression analysis, the current ratio was found to have direction a significant direction on stock returns (Lestari and Andini 2016), *current ratio* a company higher then the average value of the company is also going up, this is a positive signal for investors where more investors assess the performance and health of the company is good and buy shares so indirectly increase the value of companies in the market (Fitriana, Andini and Oemar, 2016).

*H<sub>2</sub>: Liquidity has significant influence on stock return.*

Earnings management occurs because of the disparity information received by the company outside the company, because they are the managers assume that competitors are also in line to do the same. Seeing this, the performance of competitors also in the spotlight trigger of earnings management, because of investor and creditor definitely do a comparison to determine or select a company that has seen better ratings (Indrayanti and Wirakusuma, 2017), Research conducted shows that stock returns will go up if the profit achieved by the company conform to or greater than the expected profit and vice versa, if the actual profit is smaller than expected profit then return stock is going down, so the earnings management influence on stock returns. However, different results obtained by Constancy and Adhariani (2017) found a significant positive relationship between earnings management and stock returns.

*H<sub>3</sub>: Earning management has significant influence on stock return*

## 2. Method

The population in this study are all manufacturing companies have been listed in the Indonesia Stock Exchange 2014-2018 period. Total sample of 100 companies was obtained using random sampling techniques. The data used in this research is secondary data drawn from keuangan report (annual report).

Stock return is the result obtained from the investment, it can be a return realization that has occurred or return expectations that have not occurred but are expected to occur in the future. Stock returns can be interpreted as a rate of return on the stock in line with expectations on an investment that has been made (Indrayanti and Wirakusuma, 2017), Formulated with:

$$R_t = \frac{P_t - P_{t-1}}{P_{t-1}}$$

Profitability is a tool to determine the scale of the totality of management effectiveness referring to the size of the margin levels obtained in connection with the sale and investment. In this study is proxied by the profitability ratios Return on Assets (ROA), the measurement of net profit after tax to capital. This is because the return on assets usually describes whether the shareholders receive a reasonable return on their investment (Fitriana, Andini and Oemar, 2016), Formulated with:

$$ROA = \frac{\text{Net Income}}{\text{Total Assets}}$$

Liquidity is a financial ratio that shows the capability of the organization to settle its short-term obligations that must be met. In this study, the liquidity ratio is proxied by the current ratio (CR), which is the ratio to determine the scale capability of the company in the short term to cover expenses or debts that his time runs out on the current overall billed (Wulandari, Purnomo and Murniati, 2018), Formulated with:

$$\text{Current Ratio} = \frac{\text{Current assets}}{\text{Current liabilities}}$$

Earnings management is a measure of the company's management to manipulate financial reporting process by raising or lowering the corporate profits through its policy of accounting method, it is done as a destination for personal gain. Earnings management done an act which company managers in order to influence the information in the financial statements Uswati and Barry (2016). Discretionary Accruals be a proxy of earnings management and searched using Jones Modification Model. Discretionary Accruals part modified accrual manager by using the flexibility and

freedom in the use of estimates and accounting standards. Formulated with:

$$SR = \alpha + \beta_1ROA_{1it} + \beta_2LIK_{2it} + \beta_3DAC_{3it} + \beta_4LEV_{4it} + e$$

$$DAC_t = TACT / TAT-1$$

Leverage is a ratio used to measure the extent to which the company is financed with debt. Leverage is the ratio to measure how much of the debt burden borne by the company in order to meet the asset(Sangsoko and Shaliza, 2018), With the formula:

$$DER = \frac{\text{Total Debt}}{\text{Total Equity}}$$

Data analysis using eviews analyzes the effect of profitability, liquidity, and earnings management on stock returns. The regression equation can be formulated as follows:

Information:

- SR = Stock Return
- ROA = Profitability
- LIK = Liquidity
- DACt = Profit Management
- LEV = Leverage

### 3. Result and Discussion

Once all the data and information collected phases of data processing can be immediately implemented, data processing is done with the help of program eviews 10. Based on the data processing stages that have to be obtained summary descriptive statistics of each study variable as in table 1 below:

**Table 1. Descriptive Statistic Result**

	SR	ROA	LIK	DACt	LEV
mean	0.295	0.051	2,338	-0.019	1,615
median	0,000	0,032	1,510	-0.023	0.865
maximum	44,000	3,192	49.770	1.174	162.190
Minimum	-0.990	-0.299	0,000	-0.708	-31.720
Std. Dev.	2,462	0.167	2,938	.116	8.721
Observations	500	500	500	500	500

Source: Data Processed by authors, 2023

The test results for normality using the Jarque-Bera value amounted to 2,163 with a probability 0.338. Because the probability value  $0.338 > 0.05$ , the residuals in this research model have normal distribution. The multicollinearity test can be seen from the VIF (Variance Inflation Factor) that each independent variable and the control variables used have a correlation coefficient below 10, which means the data is accessible from symptoms of multicollinearity. Heteroskedasticity test observation

probability value resulting R-squared is equal to 0,972, The results obtained showed that the probability value produced shows  $0,972 > 0.05$  so that it can be concluded that all of the variables that will be formed into a regression model has been free of symptoms heteroskedasticity. Based on the test results of the Hausman test, it can be seen that the chi-square probability is 0.779 greater than 0.05. It can be concluded that  $H_0$  accepted and models used should be Random Effect models.

**Table 3. The Results of t-test (Random Effect Model)**

Variables	coefficient	Std. Error	t-Statistic	Prob.
C	-0.764	0,039	-19.554	0,000
ROA	-0.456	0.171	-2.652	0,008
LIK	-0.014	0.009	-1.498	0.134
DACt	-0.158	0.246	-0.640	0.522
LEV	-0.000	0,003	-0.145	0.884

Source: Data Processed by authors, 2023

In table 3 it can be seen that profitability has probability value of 0.008 or less than 0.05 ( $0.008 < 0.05$ ), it can be concluded that the variable profitability is partially a significant negative effect on stock returns. This research contradicts the results of the study by Goddess (2016); (Al-Lozi & Obeidat, 2016), which indicates that ROA has a positive and significant effect on stock returns. Results of research conducted by Mande and Rate (2017) are consistent with the results of research, where ROA has a negative and significant impact on stock returns.

Variable liquidity in the table above shows that a probability value of 0.134 is more significant than 0.05 or ( $0.134 > 0.05$ ), it can be concluded that the variable liquidity partially no significant effect on stock returns. The results are consistent with research conducted by (Fitriana, Andini and Oemar, 2016); (Akbar et al., 2021); (Sucipto & Chasanah, 2019) stating that liquidity did not affect stock returns. However, contrary to the results of research conducted by Parvati and Sudiarta (2016) which states that the current ratio has a positive and significant impact on stock returns.

Earning management probability value of 0.522 is more significant than 0.05 or ( $0.522 > 0.05$ ), it can be concluded that the partial earnings management variables no significant effect on stock returns. The results are consistent with research conducted by Adiwibowo (2018) which states that profit management does not affect stock returns. However, contrary to the results of research conducted by Leon and Hwang (2019) that shows the stock return on increase or decrease stock prices showed a significant effect on stock returns of earnings management.

Leverage probability value of 0.884 or greater than 0.05 ( $0.884 < 0.05$ ), it can be concluded that the variable leverage partially no significant effect on stock returns. The results are consistent with research conducted by Slamet, Wiyono, and Murniati (2019); (Thai, 2019) which states that *leverage* does not significantly influence stock returns. However, contrary to the results of research conducted by Sangsoko and Shaliza (2018); (Edelen et al., 2016); (and Nalarreason et al., 2019) stating that leverage significant effect on stock returns.

#### 4. Conclusion

Based on data processing and discussion of hypotheses, the results showed that the profitability is partially a significant negative effect on Return Shares. Liquidity partially no significant effect on stock returns. Earnings management partially no significant effect on stock returns. and leverage no significant effect on stock returns. Profitability, liquidity, earnings management,

and leverage simultaneously significantly affect stock returns. Based on the conclusions outlined above, the researcher can put forward several suggestions as follows: It is hoped that this research can help companies, not only manufacturing companies but also other companies listed on the Indonesia Stock Exchange, to increase caution in making stock returns so that it does not become a problem. at a later time. For investors who have relationships with a company, of course they must increase supervision of management, so that they pay attention to the level of profit that investors have from a share investment made, so that investors will feel safe and avoid unwanted cases. It is better to add other variables so that the research is more meaningful and more detailed regarding the factors that influence the value of stock returns and testing other variables.

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