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THE DETERMINANTS OF STOCK PRICES: A STUDY OF FINANCIAL LISTED FIRMS IN INDONESIA CAPITAL MARKET

Adam Nurfauzi[1], Puput Dwi Jayanti[2], Zeane Siti Aminah[3], Muhammad Jodi Indrawan[4], Gusni[5]*

[12345]Management Study Program, Faculty of Economics and Business, Widyatama University, Indonesia

[1]adam.nurfauzi@widyatama.ac.id, [2]puput.dwi@widyatama.ac.id, [3]zeane.6594@widyatama.ac.id, [4]indrawan.jodi@widyatama.ac.id,[5]gusni.tanjung@widyatama.ac.id

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Keywords: stock price, determinants, financial listed firms, capital market

ABSTRACT

Knowledge about the determinants of stock prices is quite instrumental in assist investor's investmentdecisionsmaking.Thepurposeofthisstudyistoidentifythedeterminantsofshare prices in the financial listed firms at Indonesia Capital Market and show factors that investors rely on to take their investment decisions. This study using secondary data gathered from the official website of Indonesia Capital Market with the sample is 15 financial firms selected by using a purposive sampling technique for the period of 2009 – 2018. A panel data analysis method was used to investigate the determinants of stock prices in financial listed firms. The empirical research result shows that leverage has a negative effect on firm share prices, profitability and firm size have a positive effect on stock prices. Meanwhile, institutional ownership and dividend policy does not affect firm stockprices.

Keywords: stock price, determinants, financial listed firms, capital market

INTRODUCTION

Thecapitalmarketisavesselfortheinvestorstoinvestin.Onepopularinvestmentinstrument with a large number of investors in the stock. Investors make stock transactions in the capital market with a motive is to sell back their stock held at a higher price in the future, in order to obtaincapitalgain.Stockpricesalwayschangeovertime,whichisinfluencedbythepowerof demand and supply in the market. If the demand for a stock is higher, then the stock pricewill moveup,onthecontrary,iftheofferofastockishigherandthedemandislow,thentheshare

price will move down (Muflih, 2012). Changes in stock prices on the capital market occur every day that are influenced by various factors, such as company performance, leverage, ownership structure, dividend policy, company size and others (Demiralp, et. al., 2011; Bahreini, Baghbani & Bahreini, 2013; Al Qaisi, Tahtamouni, & Al Qudah, 2016; Sharif, Purohit, & Pillai, 2015; Geetha & Swaaminathan, 2015; Nasarudin, Suhendra, & Anggraini, 2019),whichcanbeusedbyinvestorstoanalyzewhetherthecompany'sconditionisprofitable ornotusedasaninvestmentvehicletogetcapitalgain.Knowledgeaboutthefirm's conditions can be used as information and references by investors in predicting stock price movements.
TheefficientcapitalmarkettheoryknownastheEfficientMarkethypothesis/EMHshowsthat investorbehaviorisrelatedtorelevantinformationreceivedbythemarket.Thistheorydefines an efficient capital market as a market whose share price reflects all relevant information so that the stock price reflects that information (Megginson,1997).

Thefirm's performanceistheinformationfortheinvestorsthatcangatherfromthecompany's financialstatementspublicationthroughcompanyfinancialratios.Brown(2004)mentionsthat financial ratios at least able to provide answers for four questions; how the companyliquidity,whether the effectiveness of management generates operating earnings on the assets, how the company will be funded, and whether common stockholders get sufficient rate of return. However, not all of the financial ratios that are used as information by the investors are the determining factors for stock prices. That is why the determinants of stock price movement especiallycomefromfirmfinancialperformancestillunclearuntilnowandstillinterestingfor furtherstudy.Theobjectiveofthisstudyistore-examinethedeterminantsoffirms'stockprices in the financial industry by adhering to the existing theory and previous research results that cancontributetothefirm'ssharepriceliteratureandimproveourunderstandingaboutfinancial company's determinants of stock prices. Although a number of previous studies have tried to illustrate the determinants of share prices, the result is stillmixed.

This study is different from other studies because it uses the financial industry which is still rarely studied in Indonesia for a period of ten years. The financial industry is very enticing to explore because of its role in driving the wheels of the country's economy. The results of this study are expected has contribute to the development of financial literature, especially related to the determinants of the firm's stock prices.

LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT LEVERAGE AND STOCK PRICES

Lay down corporate leverage is clearly the responsibility of managers because changes in leverage will affect financial capacity, investment risk, strategic choices, and the level of investor wealth through changes in stock prices (Bahreini, Baghbani & Bahreini, 2013). The company should set a target of composition debt in the firm capital structure to gets a stable share price and better future prospects (Iqbal, et. al, 2016). Trade-off theory (Modigliani & Miller, 1863) states that companies must determine the optimal leverage ratio, any deviation (increase or decrease) from the optimal level of leverage will have a negative impact on the company's stock price. The use of debt in the company's capital structure is also very closely related to debt

management itself. The higher the level of debt held by the company without beingfollowedbygoodmanagementwillpushthecompanyfacingbankruptcyorexperiencing financial distress. If this condition occurs, it can be ensured that the share price will continue to decline, so that it can cause investors to get a loss (capitalloss).

Anumberofresearchshowthatthereisanegativeeffectofleverageonthestockprice(Eckbo, Masulis,&Norli,2007;Hussain&Gull.,2011;Korteweg,2004;Penman,Richardson&Tuna, 2007; Iqbal, et. al., 2016). Research conduct by Nirmala et al. (2011); Olowe & Uwuigbe (2012) found that leverage has a positive effect on the firms shareprices.
Hypothesis 1: Leverage has a negative effect on the financial listing firms stock price

PROFITABILITY AND STOCK PRICES

Profitability has important role in describing firm future. Profitability indicate firm capability to produce profit which can be used to extend the company's business (Purnamawati, 2016).If thecapitalmarketisinasemi-strongefficientmarketcondition,nooneinvestorwillobtainan abnormal return based on general information, then the stock price will reflect changes in profits generated by the company which shows that the stock market can accurately predict variationsincorporateearningsbeforeitisannouncedtothepublicandimpactonstockprices (Su, 2003). Balsam & lipka, 1998 explain that future profitability and share price determined by rational expectations, that why profitability able to explain stock price. Profitability ratios indicate the level of management effectiveness in managing the company as seen from the returns generated from sales and investment activities (Purnamawati, 2016). Highprofitability has an attraction for the investors because it shows the better performance of companies that haveanimpactonrisingstockprices.Anumberofpreviousresearchshowthatprofitabilityhave a positive effect on the firm's stock prices (Ball & Brown, 1968; Malhotra & Tandon,
2013;Almumani,2014;Purnamawati,2016;Bayrakdaroglueta l.,2017).Otherresearchresult show that there is negative relationship between profitability and stock price (Susilowati, 2015).

Hypothesis 2: Profitability has a positive effect on the financial listing firms stock price.

INSTITUTIONAL OWNERSHIP AND STOCK PRICES

Empirical evidence about the relationship between stock price and the firm's ownership
structurehasbeenwidelydiscussedinthefinancialliterature.Institutionalownershipisastock that is owned by an institution or organization and is not an individual stock (Yulianto, 2014). The firm ownership structure can be divided into two, namely a concentrated ownership structureandadispersedownershipstructure(Saif,et.al,2013).Institutionalshareholderswith a large number of shares have stronger monitoring related to corporate management decision making. High levels of institutional shareholder ownership are often seen as positive news about the company's long-term prospects (Chemmanur et al., 2009). A good management performance believed can increase the company's stock price. Barber (2007) informs that the company's profit increase was more than $ 3 billion because it had large institutional shareholders. Chen, et al. (2007) shows that in the case of mergers, the withdrawal of unfavorable bids is likely to occur to companies with independent long-term institutional investors.Aggarwaletal.(2010)mentionthatcompanieswithhighinstitutionalownershipar

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morelikelytolimitthepoorperformanceoftopmanagementwhichwillincreaseinvestortrust. Research conduct by Kurniawati, et al. (2015); Gompers & Metrick (1999); Osagie, Osho, & Sutton (2005) show that institutional ownership has a positive impact on firm stock prices. Meanwhile, Haghighat, et al. (2015) found that institutional ownership has a negative impact on the firm stockprice.

Hypothesis 3: Institutional ownership has a positive effect on the financial listing firms stock price

DIVIDEND POLICY AND STOCK PRICES

The company will distribute cash dividends or stock dividends to shareholders sourced from thecompany'sprofits(McLaney,2009).Dividenddistributiondependsontheprofitearnedon the current time and is part of the dividend in the previous year (Lintner, 1956). Investors buy shares with the aim of obtaining capital gains and dividends, but the dividend is not promised (Gitman, 2009). Investors are making dividends as the basis for valuing stock prices, considering that dividends are the only cash payments received by shareholders directly from thecompany.Stockpricesoftenrespondtounexpectedchangesindividendsatannouncements (Denis et al., 1994). Companies that make changes in dividend policy may experience increasing or decreasing of stock return trends (Gunasekarage et al., 2006). Affleck-Graves & Mendenhall (1992), mention that the share price will react to the company's earnings announcement. Firms that pay more dividends will have an increased share value, while a company with low dividend policy will run into undervalued (Hampton, 1996). A number of previous research found a positive correlation between dividend policy and firms stock prices (Benartzietal.,1997;Bae,1996;AlMasum,2014;Attah-Botchwey,2014).Otherstudiesshow that dividend policy has a negative effect on firms' stock prices (Hashemijoo, et al.,2012).

Hypothesis 4: Dividend policy has a positive effect on the financial listing firms stock price

FIRM SIZE AND STOCK PRICES

The firm’s size describes the dimension of a company that can be valued from the total assets owned, average assets, total sales, and average total sales. Empirical evidence shows thatompany size has a positive relationship with share prices. The greater the size of a company, thegreaterthecompany'sabilitytomaximizecompanyprofitsandthegreaterofinvestortrust. Firm size is one of investor consideration before making an investment decision (Handayani, et. al, 2019). Company size reflects the company's ability to deal with risks and access to external funding sources. Large companies tend to be more popular among investors because they are considered capable of providing relatively stable returns. A number of studies show that firm size has a positive effect on firm stock price (Acheampong et al., 2014; Ayuba, et l, 2019; Duy & Phuoc, 2016; Hidayat,2016).

Hypothesis 5: Firm size has a positive effect on the financial listing firms stock price

RESEARCH METHODOLOGY

The type of this research is applied research with a quantitative approach. The data for the studywasgatheredfromtheofficialwebsiteoftheIndonesiaStockExchange(www.idx.co.id) andcompanyannualreport.Thedatawassecondarydataintheformofdocumentsonfinancial statements and other related information such as company annual report and share statistic report. This research used companies in the financial industry listed at the Indonesia stock exchange consist of 79 companies and the companies divide under the categories of the bank, financial institution, securities company, insurance, investment fund/mutual fund, and others. Panel data for the study collected from the period of 2009 -2018 which samples were taken from15companiesbyusingapurposivesamplingtechnique.Paneldatagivemoreinformative data, more variability, less collinearity among the variables, more degrees of freedom, and moreefficiency.
All variables used in this study and their measurements can be seen in table 1 below:

Tabel 1. Research variable and measurement

Variables	Measurements	Symbol
Independent variables		
Leverage	Total debt/Total Assets	Lev
Profitability	Earnings after tax/Total Assets	Profit
Institutional Ownership	Institutional ownership/number of share outstanding	IO
Dividend Policy	Dividend per share/earnings per share	DP
Firm Size	Ln Total Asset	Size
Dependent variable		
Stock Price	Closing share price at 31st December for the years studied	SP

The panel data regression model used in this research was adopted from the regression model thathasbeenappliedbySharif,Purohit,&Pillai(2015)toanswertheresearchhypotheseswith the following regressionequation:

$$SP = a + \beta 1Lev + \beta 2Profit + \beta 3IO + \beta 4DP + \beta 5Size + e$$

Where a was constanta, β1, β2, β3, β4, β5 were regression coefficients, and the variables already being defined in table 1 above.

Panel data regression testing starts with the classic assumption test consisting of a multicollinearity test and a heteroskedasticity test. The aim of the test is to ensure that the formed regression equation model has accuracy in estimation, is unbiased and

consistent. Thenext step is the regression model test which consists of the F and coefficient of determination test to find out whether the model formed is fixed and the independent variables used in this research are able to interpret changes in the dependent variable. The last test conducted was thehypothesistest(t-test)tofindoutwhethereachindependentvariableusedinthisstudyhad an influence or not on the dependent variable with an error rate of5%.

RESULT AND DISCUSSION RESULT

Multicollinearity test results indicate that there is no multicollinearity problem between independent variables or all independent variables in the regression model of this study have been mutually independent because of the value of Variance Inflation Factor (VIF) <10 (see table 2). Heteroskedasticity test results by using the White test showed that P-value obs * R- square of 0.0595> 0.05, which means there is no heteroscedasticity problem in the research regression model.

Paneldataregressionhasthreemodels:commoneffects,fixedeffects,andrandomeffects.The results of the regression model selection by using Chow, Hausman, and Lagrange Multiplier tests indicate that the random effect model is the most suitable for this study because it uses more cross-section data than time-series data (Nachrowi and Usman, 2006). Panel data regression test results can be seen in the following table2:

Table 2. Panel data regression and multicollinearity test results

Independent Variables	Regression Coefficient	Multicollinearity (VIF)
Leverage	-0.3019**	1.77
Profitability	6.7156***	2.11
Institutional ownership	-0.1973	1.04
Dividend policy	0.4137*	1.08
Firm size	0.3601***	1.30
Adjusted R^2	0.2656	
F-statistic	11.7785	
Prob F-statistic	0.0000	

*** Significant at 1%, **5%, *10%
Source: Financial statements, capital market statistic, data processed

Statistical test results show that the regression model was fixed which is seen from the value of Prob F-statistic <0.05, meaning that there is a linear relationship between the independent variables (leverage, profitability, institutional ownership, dividend policy, and firm size) with the dependent variable (stock price). The coefficient of determination test explains that the ability of the independent variable in interpreting changes in the dependent variable is26.56% (adjustedR^2value),theremaining73.44%isexplainedbyothervariablesnotusedinthisstudy.

The results of the hypothesis test (t-test) as seen in table 2 above explained that the leverage variable has a negative effect, the profitability, dividend policy and firm size variables have a

positiveeffectonthefirmstockprices.Anothervariable(institutionalownership)hasnoeffect on the firm stock prices of financial industry listed firm on the Indonesian capitalmarket.

DISCUSSION

Leverage describes how much the use of debt in the company's capital structure. High-level use of debt in a firm capital structure not good for the company, especially if not managed properly can cause the company to go bankrupt. Hypothesis test results indicate that leverage has a negative influence on firm stock prices of the financial industry listed in the Indonesiacapital market for the period 2009 – 2018. This study result suitable with trade-off theory (Modigliani & Miller, 1863) mentions that companies who have any deviation (increase or decrease) from the optimal level of leverage will have a negative impact on the company's stock price. Investors prefer companies that have low debt because they have low risk, especially in the current unstable economic conditions.

This research result in line with the study performed by Eckbo, Masulis, & Norli, 2007; Hussain & Gull., 2011; Korteweg, 2004; Penman, Richardson & Tuna, 2007; Iqbal, et. al., 2016,andnotinlinewithresearchconductbyNirmalaetal.(2011);Olowe&Uwuigbe(2012) that found leverage has a positive effect on the firms shareprices.

Profitability describes the firm capability to generate profit from all investments made by the company. The increase in profitability achieved by the company indicates the enhancement of management effectiveness in managing company investment activities. Hypothesis testresults show that profitability has a positive effect on firm stock prices. This condition describes that the higher level of the company's ability to generate profits, then the higher of investor's trust that will cause a rise in the company's stock price, on the contrary, the lower level of the company's profit, then the lower of the market's appreciation for the company, causing the stock price going down. The company's ability to generate high profits level is good news for the investors which also points that the company has better prospects in thefuture.

This research result suitable with study conduct by Ball & Brown, 1968; Malhotra & Tandon, 2013; Almumani, 2014; Purnamawati, 2016; Bayrakdaroglu et al., 2017), and contrary with research performed by Susilowati, 2015, found there is a negative relationship between profitability and stock price.

Institutional ownership with a large number of shares has an important role in the company's corporate governance, especially related to its ability to conduct supervision, gather information, and the impact on the company policies and performance. Statistical test results show that institutional ownership has no effect on the stock price. It's mean that high or low levels of institutional ownership composition in the company unable to increase or decrease the firm stock prices. This condition illustrates that the role of institutional investors has mentioned in agency theory still not maximized in the financial industry during the study period. This study result not in line with research conduct by Kurniawati, et al. (2015); Gompers & Metrick (1999); Osagie, Osho, & Sutton (2005) show that institutional ownership has a positive impact on firm stock prices.

The dividend has a function as information transmitter to the investor about the firm's performancethatmakesthecapitalmarketreactpositivelyasstatedbyMegginson(1997)who said that when the firm announces dividend increases, then the stock's price will increase by onetothreepercent,converselywhenthefirmreducesorgetridofthedividend,thenthestock pricewilldeclineupto50%.Hypothesistestresultsindicatethatdividendpolicyhasapositive effect on the firm stock prices. This condition indicates that the greater amount of dividends distributed to the investors, the higher the investor's confidence to the company's prospects in thefutureandtheincreasingsharepriceofthecompanyasaresultoffirmhighstockdemand. This research in line with the research result of Benartzi et al., 1997; Bae, 1996; Al Masum, 2014; Attah-Botchwey, 2014, and contrary to research conduct by Hashemijoo, et al.,2012.

Company size describes the ability and strength of the company. The greater size of the company, then the greater the assets owned by the company's which indicate the greater ofthe company'spowertoimprovecompanyperformancewhichhasanimpactonincreasinginvestor confidence in the company's future prospects. High investor trust will push firm stock prices tocontinuetoincrease.Statisticaltestresultsshowthatfirmsizehasapositiveeffectonthefirm stockprice.It'smeanthegreatersizeofthefirmthenthehigherpriceoffirmstockprices. Company size reflects the company's ability to deal with risks and access to external funding sources. Large companies tend to be more popular among investors because they are considered capable of providing relatively stable returns. This research result in line with studies performed by Acheampong et al., 2014; Ayuba, et l, 2019; Duy & Phuoc, 2016; Hidayat,2016.

CONCLUSION

The purpose of this study is to determine the determinants of stock prices in the financial industry that are listed on the Indonesian capital market. The results of the study illustrate that the variable leverage has a negative influence on the company's stock price and profitability, dividend policy & firm size have a positive relationship with the company's stock price. Another variable, institutional ownership has no influence on the company's capital structure. This condition illustrates that not all variables used as determinants of the company's stock price have an influence on changes in stock prices in financial companies listed on the Indonesian capital market. Although there are 4 variables out of the 5 variables used in this study that have an influence on stock prices, their ability to explain changes in stock prices in the financial industry is still weak as seen from the coefficient of determination.

This research still has a number of limitations that might have an impact on the results of the study. First, this research only uses financial companies listed in the Indonesia capital market as a sample with a limited number of samples (15) during the period of 2009-2018. Second, this study still uses limited independent variables, only five independent variables. Therefore it is suggested to other researchers to use a wider sample and more independent variables in accordance with the theory and previous research.

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