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THE IMPACTS OF PROFITABILITY, LIQUIDITY, FREE CASH FLOW AND SET OPPORTUNITY OF INVESTMENT TO DIVIDEND AND ITS IMPACT ON ABNORMAL RETURN

(Empirical Study of Mining Companies Registered on Indonesia Stock Exchange)

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ABSTRACT

This study aimed at examining the impacts of profitability, liquidity, free cash flow, and set of investment opportunities to dividends and their impact on abnormal return either simultaneously or partially. The population in this study covered 41 mining companies registered on the Indonesia Stock Exchange during the period of 2011-2015 abnormal return of 41 mining companies registered in Indonesia Stock Exchange. Horizon time in this study is a combination of cross sectional studies with longitudinal (time series) called the panel data or pooled data. This study uses a panel type data balance (balance panel data). The method of analysis used in this research is path analysis method (path analysis). Sample size was obtained as many as 21 samples. The results of the research prove that 1) profitability, liquidity, free cash flow and investment opportunity sets together affect dividend, 2) profitability and investment opportunity sets affect dividend, 3) liquidity and free cash flow negatively affect dividend, 4) profitability and liquidity negatively affect abnormal return, 5) free cash flow and investment opportunity sets affect abnormal return, 6) dividend effect on abnormal return, 7) profitability, liquidity, free cash flow, and investment opportunity sets together effect to abnormal returns through dividends, 8) profitability and set of investment opportunities with an abnormal return through dividends, and 9) liquidity and free cash flow sets negatively affect the abnormal return through dividends.

Keywords: Profitability, Liquidity, Free Cash Flow, Investment Opportunity Set, Dividend and Abnormal Return

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1. INTRODUCTION

Today's business development shows that every company has a competitive competition, whether from the trade, services, industry, and mining. Such operations require funding sources and utilization of other supporting production sources for the sustainability of the company's operations. The utilization of the company's resources should be done effectively and efficiently so that it can increase the value and performance of the company. Funding problems within the company are one of the most important issues faced by every company, from fund withdrawals to the allocation of funds effectively and efficiently (Mutia and Arfan, 2010).

Capital market is one of the institutions that play an important role in an economy and it is a solution for investors to choose to invest (Machfiro and Sukoharsono, 2011). According to Hatta and Dwiyanto (2012), the main activity of the capital market is to bring together the party experiencing lack of funds with those who have excess funds with a securities broker (lender to borrower). The main objective of an investor in investing funds is to obtain income (return), both in the form of dividend income (dividend yield) as well as income from the difference between the selling price of shares and the purchase price (capital gain).

In Indonesia, mining companies are the world's top six in terms of ownership of mining materials. But in terms of the investment climate, Indonesia is in the bottom of the line. Indonesia has top potential minerals for coal. It reached the 3rd rank for coal exports, ranked 2nd for tin production, 2nd for copper production, 6th for gold production. This excellent tectonic and geological condition that brings Indonesia to become one of the largest producers of gold, copper, tin and nickel. Indonesia is able to contribute the largest gold reserves in South East Asia, which amounted to 39%.

Dividends are influenced by returns generated by the company in performing its activities. Investors in investing their capital, besides based on information of trend of stock movement officially issued by BEI, they will also see company profile, especially factors that can be measured in yield return to stock. Normal return is a thing that is expected by all investors in investing in a company. But in a capital market, it is possible that the opposite occurs, that the expected normal return does not occur. This is called longtime abnormal return. This abnormal return can be above average and can also be below the average that usually occurs in the stock market. Tony (2012) in Ida (2002), investor rationality can be measured from the extent to which they succeed in selecting stocks that deliver maximum results with certain risks or certain results with minimum risk.

Abnormal return is the result of a reduction of the pure profit value obtained by the investor and the expected return on investment. Returns may change according to the economic events that

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occur, or because stock prices are constantly changing (Andreani and Christina, 2014). Abnormal return is defined as the rate of return generated by the stock or portfolio during a certain period, where the rate of return is different from the expected rate of return. Expected Rate of Return itself is defined as the expected rate of return with some valuation methods such as asset pricing model using historical data, in the long run, to make the results more accurate (Listyo, 2009). The study of events analyzes the abnormal return securities that may occur around the announcement of an event (Jogiyanto, 2005). In general, abnormal return is a return whose value exceeds the normal return value so that all investors want to get the abnormal stock return. Adhe and Bandi (2015) in Ardiawan (2015) stated that market reaction can be measured by looking at the abnormal return of shares received by investors.

The first factor which is believed to affect the abnormal return is dividends. Dividends are the share of profits to shareholders based on the number of shares owned and are one of the information that attracted the attention of investors. This payment will reduce the retained earnings and cash available to the company, but the distribution of profits to the owners is indeed the main objective of a business. Nugroho's research (2014) in Adhe and Bandi (2015) states that there is no market reaction before and after the announcement of a fixed dividend with an abnormal return indicator. Research on previous dividends has been also carried out by Ghulam (2012), Pratita (2013), Anggi et.al, (2015) Adhe and Bandi (2015) and Risha (2015).

The second factor that is expected to affect the abnormal return is profitability. Profitability shows the company's performance in generating profit. The indicators used are ROA (Return On Assets). According to Partington (1989), the profitability ratio shows the company's success in generating profits. If the demand for stocks increases then the stock price will tend to increase, this will result in increased stock return which means profitability have a significant positive effect on the company's return above the expected return. Research on previous profitability was carried out by Islam, et.al, (2012), Ida and Sudiarta (2013), Yudhanto and Aisjah (2013), Salvatore and Putu (2014), positively affect dividends and Brian and Suarjaya (2013).

The third factor that is expected to affect the abnormal return is liquidity. Liquidity is an indicator in measuring the ability or health of the company in meeting its obligations, both short-term debt, and long-term debt. According to Usman (1990: 155), the financial ratios that can affect stock returns are liquidity ratios, because a company with large debts can reduce dividends paid to shareholders, so investors do not want to invest in the company which causes the stock price to decline. The more liquid a company then most likely the company will pay greater dividends as well. The research on liquidity was conducted by Suharli (2007), Idawati and Sudiartha (2013), Brian and Suarjaya (2013), and Tony (2012).

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The fourth factor that is expected to affect abnormal return is free cash flow. Free cash flow is excessed cash in the company that can be distributed to shareholders in the form of dividends (Bringham and Daves, 2003). The division can be done after the company does capital expenditure, for example, the purchase of fixed assets in cash. According to Ross et al (2000) in Susilawati (2010) that there is a difference of interest between shareholders and managers in managing free cash flow. The study of the effect of free cash flow was conducted by Metha and Barbara (2011), Ferry (2011), Trilas and Arfan (2013), Sindhu (2014), and Salvatore and Sugiartha (2014).

The fifth factor considered to affect the abnormal return is the Investment Opportunity Set (IOS). Companies with growth rates are often also regarded to have high investment opportunity sets (Subekti and Kusuma, 2001). It is very motivating for the managerial to reinvest in a large amount. With increasing growth, the company prefers to use more funding sources from internal companies compared to external sources of funds (issuance of shares or bonds). The risks and costs of internal sourced funds are preferred and lower and cause a decrease in dividends to be distributed to shareholders (Myers and Majluf, 1984). Research Dewi and Suaryana (2013) have a positive effect on the growth of companies that have implications for the return company. This research was also conducted by Ferry (2011), Dewi and Suaryana (2013), Salvatore and Sugiartha (2014). And Adi and Gerianta (2016).

The purpose of this study is to examine the impact of profitability, liquidity, free cash flow, and set of investment opportunities to dividend an impact on abnormal return, either simultaneously or partially.

2. RESEARCH METHOD

This was hypothesis research. The units of analysis used covered 41 mining companies listed on the Indonesia Stock Exchange during 2011-2015. The time horizon in this study was a combination of cross-sectional studies with longitudinal (time-series) called data panels or pooled data (Gujarati, 2003). This study used a balanced panel data. According to Gujarati (2003), panel data is a balanced panel of data that each unit of the object (cross-section) has the same amount of time series data. The level of intervention in this study was minimal intervention. The population of this study comprised of 41 mining companies registered on the Indonesia Stock Exchange for the period of 2011-2015. The sample selection in this research was done through purposive sampling method which selected 21 companies registered in 41 mining companies during the period of 2011-2015 so that the sample size in this research is 105 observation. The data source used as primary data and data collection technique used was documentation.

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The method of analysis used in this research was path analysis method. The method formed in this analysis was used to explain the magnitude of influence (not predict) independent variable to the dependent variable.

3. RESULTS AND DISCUSSION

The Effect of Profitability, Liquidity, Free Cash Flow, and Investment Opportunity Sets together affect Dividend

Based on the research, it can be explained that the influence of profitability, liquidity, free cash flow, and investment opportunity simultaneously affect the dividend of mining companies listed on Indonesia Stock Exchange. The magnitude of the simultaneous influence of these four variables can be seen from the value of the coefficient of determination. The coefficient of determination influence of four variable that is profitability, liquidity, free cash flow, and set of investment opportunity to dividend is equal to 0.123, meaning 12.3% change in dividend can be explained by change from profitability, liquidity, free cash flow and opportunity investment, while the rest of 87.7% is explained by other factors outside the variables of profitability, liquidity, free cash flow, and investment opportunity set. These results show that profitability, liquidity, free cash flow, and investment opportunity sets have a less powerful effect on corporate dividends.

Impact of Profitability Partially on Dividends

The result of the research shows that profitability has an impact on the dividend in mining company listed in Indonesia Stock Exchange with coefficient value 0,228, it means that every change to profitability variable equal to 1 unit, it will increase dividend equal to 0,228. The result of this research proves that profitability influence to increase the dividend. The greater the profitability of the company will be the greater the dividends earned, which will lead to an increase in stock demand.

The results of this study are in line with the results of research conducted by Idawati and Sudiarta (2013) which states that profitability has a positive effect on dividend policy. The same is also expressed Salvatore and Sugiarta (2014) in his research, where researchers found that profitability has a positive effect on dividend payout ratio policy. This means that the higher level of profitability of the company will affect the increase in demand for stocks.

Impact of Liquidity partially on Dividends

The result of this research shows that liquidity had an influence to the dividend in mining

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company listed in Indonesia Stock Exchange with the coefficient value equal to -0.029, meaning every change to liquidity variable equal to 1 unit, it will decrease dividend equal to 0.029. The results of this study proved that liquidity had a negative effect on dividends. The results of this study were consistent with the results of research conducted by Idawati and Sudiarta (2013) which states that liquidity affects dividends. This shows that the liquidity ratio has an important role in the decision taken by investors to invest. Liquidity ratio is expected to be as low as possible, so it will affect the stock return. This then affects investors who are interested in investing in the company. This is expected to have an impact on increasing the company's return so that the dividends earned will also increase. But this research is not in line with the results of research conducted by Brian and Suarjaya (2013), where researchers found that liquidity has no impact on stock return.

Impact of Free Cash Flow partially on Dividend

The results showed that free cash flow has an effect on dividend on the mining company listed on the Indonesia Stock Exchange with a coefficient of - 0.1, meaning that any change to the free cash flow variable of 1 unit, it will reduce the dividend by 0.1%. The results of this study prove that free cash flow has a negative effect on dividends. This may happen, given the possibility of different interests between shareholders and managers in managing free cash flow. The results of this study are not in line with the results of research conducted by Adi and Gerianta (2016) which states that free cash flow has a positive effect on dividend policy. The results are also in line with Metha and Barbara (2011) and Trilas and Arfan (2013) studies which stated that free cash flow has a positive effect on dividend policy. Other research results that are different from the above research is the research of Salvatore and Sugiarta (2014) stating that free cash flow does not affect dividend payout ratio. In addition, other studies that found similar decisions were studies conducted by Sindhu (2014) and Ferri (2011).

Impact of Investment Opportunity Set on Dividend

The results showed that investment opportunity sets have an effect on dividend on mining companies listed in Indonesia Stock Exchange with a coefficient value of 0.226, meaning that any change to profitability variable of 1 unit, it will increase dividend equal to 0,226%. The results of this study prove that the set of investment opportunities affect the increase in dividends. The results of this study are consistent with the results of research conducted by Adi and Gerianta (2016) stating that the investment opportunity set has a positive effect on dividends. The results also support the Ferry (2011) study which states that investment opportunity sets affect the dividend policy. This indicates that investment opportunity sets also play an important role in improving corporate earnings. Firms with high investment opportunity sets will motivate

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managers to re-invest in large numbers. This is then the implications for the return company. However, the results of this study are different from the research of Salvatore and Sugiarta (2014) which states that the investment opportunity set does not affect the dividend payout ratio.

Impact of Profitability on Abnormal Return

The results showed that profitability has an effect on abnormal return on mining company listed in Indonesia Stock Exchange with a coefficient value equal to -0.055, meaning that every change to profitability variable equal to 1 unit, it will decrease abnormal return equal to 0.055%. The results of this study indicate that profitability negatively affects the abnormal return. This indicates that the increase in profitability experienced by mining listed in Indonesia Stock Exchange has no effect on the increase of abnormal return received by the company. This is very likely to happen where the current return is close to the expected return, so it will have an impact on the small abnormal return earned. It indicates that the firms that tested already have a returning scheme that is populated. The results of this study are not in line with the results of research conducted by Idawati and Sudiarta (2013) which states that profitability has a positive effect on dividend policy. The same is also expressed Salvatore and Sugiarta (2014) in his research, where researchers found that profitability has a positive effect on dividend payout ratio policy.

Impact of Liquidity on Abnormal Return

The result of the research shows that liquidity has an effect on abnormal return on mining company listed on Indonesia Stock Exchange with a coefficient value equal to -0.392, meaning that any change to liquidity variable equal to 1 unit, it will decrease abnormal return equal to 0,392%. The results of this study prove that liquidity negatively affects the abnormal return. This is similar to the explanation in the discussion 4.2.3, where the increase in the liquidity ratio of a company will have an impact on the decrease in investor desire to invest in the company. This will then affect the decrease in returns obtained by the company, so it also affects the decrease in the level of abnormal return. But the results of this study is not in line with the results of research conducted by Tony (2012) which states that liquidity does not affect the abnormal return.

Impact of Free Cash Flow on Abnormal Return

The results showed that free cash flow has an effect on abnormal return on mining company listed in Indonesia Stock Exchange with a coefficient value equal to 0,061, meaning that any change to free cash flow variable equal to 1 unit, it will increase abnormal return equal to 0,061%. The results of this study prove that free cash flow effect on the increase of abnormal return. This indicates that free cash flow is also used as a basis for decisions taken by investors.

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Where the free cash flow of large companies will have an impact on increasing investment interest, so that will impact on increasing returns obtained by the company. The results obtained are in line with the results of research conducted by Adi and Gerianta (2016) which states that free cash flow has a positive effect on dividend policy. The results are also in line with Metha and Barbara (2011) and Trilas and Arfan (2013) studies which stated that free cash flow has a positive effect on dividend policy.

Impact of Investment Opportunity Set on Abnormal Return

The result of the research shows that investment opportunity sets have an effect on abnormal return on the mining company listed in Indonesia Stock Exchange with a coefficient value of 0.16, it means that any change to investment opportunity set of 1 unit will increase the abnormal return of 0.16 %. The results of this study prove that investment opportunity sets have a positive effect on the increase of abnormal return. This suggests that the investment opportunity set has a role in increasing the company's abnormal return. This happens because the increased set of investment opportunities resulted in the company managerial will do a big re-investment. This then affects the increase in return obtained by the company. So as to enable earnings obtained by the company will be greater than expected return or experiencing abnormal return.

Impact of Dividend on Abnormal Return

The result of the research shows that dividend has an effect on abnormal return on mining company listed in Indonesia Stock Exchange with a coefficient value equal to 0,571, it means that every change to dividend variable is 1 unit, it will increase abnormal return equal to 0,571%. The results of this study prove that the dividend positive effect on the increase abnormal return. These results prove that dividends have an important role in the calculation of abnormal return of a company. Where profit sharing to shareholders will impact on retained earnings and cash available in the company. This then also resulted in the abnormal return earned by the company.

Impact of Profitability, Liquidity, Free Cash Flow, Investment Opportunity Set, and Dividend together on Abnormal Return

The result of the research shows that simultaneously profitability, liquidity, free ka, and investment opportunity, and dividend have an effect on to abnormal return at mining company listed in Indonesia Stock Exchange. It is indicated by the value of Fcount> Ftable (7.018> 2.33) at the 5% significance level. The results of this study imply that the variables of profitability, liquidity, free cash flow, investment opportunity set, and dividend simultaneously affect the abnormal return of mining companies which is listed on the Indonesia Stock Exchange. The magnitude of the simultaneous influence of these five variables can also be seen from the

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coefficient of determination. The coefficient of determination influence of these four variables to the abnormal return is 0.501, meaning 50.1% change in variable abnormal return can be explained by changes in the variable profitability, liquidity, free cash flow, investment opportunity set, and dividend while the rest of 49.9 % can be explained by other factors beyond the variable profitability, liquidity, free cash flow, investment opportunity set, and dividends.

Dividends Mediating Profitability on Abnormal Return

The direct effect of profitability on dividends is 0.13 and the indirect effect of profitability on dividends is 0.405, this indicates that the direct effect of profitability is less than indirect influence. Thus the influence of profitability indirectly more able to increase dividend of mining companies listed on Indonesia Stock Exchange. The results of research can be explained that profitability partially significant effect on abnormal return companies listed on the Indonesia Stock Exchange. The result of this research gives the implication that profitability has positive influence to abnormal return through dividend as a coefficient value of path ρyx (X1 to Y) or ρyz (Y to Z) ≠ 0, then based on the result of test obtained value 0,228 and 0,571. For the value of ρyx1 x ρyz is 0.13 < 0.405, then Y mediates partially affects X1 on Z or dividend partially mediates the effect of profitability on the abnormal return. This proves that with higher profitability will give effect to the increase of abnormal return through company dividend level.

Impacts of Dividends Mediating Liquidity on Abnormal Return

The direct effect of liquidity on dividends is -0.02 and the indirect effect of liquidity to dividends is 0.405, this indicates that the direct effect of liquidity is less than indirect influence. Thus the influence of liquidity indirectly more able to increase dividend Mining companies listed on the Indonesia Stock Exchange. Based on the results, it can be explained that liquidity partially significant effect on abnormal return companies listed on the Indonesia Stock Exchange. The result of this research give the implication that liquidity has positive influence to abnormal return through dividend as a coefficient value of path ρyx (X2 to Y) or ρyz (Y to Z) ≠ 0, then based on test result obtained value -0.029 and 0.571. For the value of ρyx2 x ρyz is -0.02 <0.405, then Y mediates partially the effect of X2 on Z or dividend partially mediates the effect of liquidity on the abnormal return. This proves that with the higher liquidity will give effect to the increase of abnormal return through company dividend level.

Impact of Dividends Mediating Free Cash Flow on Abnormal Return

The immediate effect of free cash flow to dividends is -0.06 and the indirect effect of free cash flow to dividends is 0.405, this indicates that the direct effect of free cash flow is less than the indirect effect. Thus the effect of free cash flow indirectly more able to increase dividend of

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mining companies listed on Indonesia Stock Exchange. The results can be explained that the free cash flow partially significant effect on abnormal return companies listed on the Indonesia Stock Exchange. The results of this study imply that free cash flow has a negative effect on the abnormal return through dividend as the coefficient value of path ρyx (X3 to Y) or ρyz (Y to Z) ≠ 0, then based on the test results obtained value -0.1 and 0.571. For the value of ρyx3 x ρyz is -0.1 <0.405, then Y mediates partially the effect of X3 on Z or dividend partially mediates the effect of free cash flow to abnormal return. This proves that with the higher free cash flow will give effect to the increase of abnormal return through company dividend level.

Impact of Dividend Mediating Investment Opportunity Set on Abnormal Return

The immediate effect of the investment opportunity set against dividend is 0.129 and the indirect effect of the investment opportunity set against dividend is 0.405, this indicates that the direct effect of the investment opportunity set is smaller than the indirect effect. Thus the effect of investment opportunity sets is indirectly more able to increase the dividend of mining companies listed on the Indonesia Stock Exchange. The results can be explained that the investment opportunity set partially significant effect on abnormal return companies listed on the Indonesia Stock Exchange. The result of this research gives the implication that investment opportunity set has positive influence to abnormal return through dividend as a coefficient value of path ρyx (X4 to Y) or ρyz (Y to Z) ≠ 0, then based on test result obtained value 0,226 and 0,571. For the value of ρyx4 x ρyz is 0.129 <0.405, then Y mediates partially the effect of X4 on Z or dividend partially mediates the effect of the investment opportunity set against the abnormal return. This proves that with the higher set of investment opportunities will give effect to the increase of abnormal return through company dividend level.

4. CONCLUSION AND SUGGESTION

Conclusion

The results show that profitability, liquidity, free cash flow, and investment opportunity simultaneously affect the dividend on 41 mining companies listed on the Indonesia Stock Exchange. And the result of research proves that simultaneously profitability, liquidity, free ka, and investment opportunity, and dividend affect abnormal return on 41 mining companies listed in Indonesia Stock Exchange.

Suggestion

For academic development, it is suggested that more researcher intensify research focusing on variable profitability, liquidity, free cash flow, and set of investment opportunities associated

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with an abnormal return. It is also expected that there will be more study examining variables that are strongly suspected to affect dividends. Further research can also be developed again in the form of qualitative research so that factors that affect dividend and abnormal return so that it can provide more information regarding the subject matter.

