

INVESTMENT OPPORTUNITY AND PERFORMANCE OF MANUFACTURING COMPANY IN INDONESIA

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Abstract: This study aims to examine and explain the effect of Market to Book Value of Equity, Ratio of Depreciation to Firm Value, and Ratio of capital expenditure to book value of assets simultaneously to company performance are proxied by return on investment (ROI). In addition, this study also aims to determine the most dominant influence. The sample used in this study are 8 companies of Textile and Garment Sub-sector which go public in Indonesia Stock Exchange and got a total of 40 pooling data for period 2010-2014. This study uses the method of financial ratio analysis, descriptive statistical analysis, and inferential statistical analysis. The result of the study shows that the contribution of Market to Book Value of Equity, Ratio of Depreciation to Firm Value, and Ratio of capital expenditure to book value of assets simultaneously to company performance are proxied by return on investment (ROI) equal to 42.2%. Estimation results can be seen that the variable that has the largest standardization coefficient is the variable Market to Book Value of Equity. Thus, Market to Book Value of Equity has the most dominant influence on return on investment (ROI).

Keywords: Investment Opportunities, Corporate Performance, Manufacturing Company.

The investment decision is an important factor in the corporate finance function. Company performance is determined by investment decisions. The opinion can be interpreted that the investment decision is important because to achieve corporate goals that can only be generated through corporate investment activities. Investment opportunity sets are crucial for improving corporate performance. This is in accordance with stakeholder theory. Empirically, it has also been proven by Cho (1998) and Ehie and Olibe (2010), in their study

that has examined the effect of investment opportunity sets on firm performance. The influence of investment opportunity sets on company performance is also based on signaling theory and asymmetric information (Myers and Majluf, 1984). The bigger the investment opportunity set, the greater the company's debt because the creditor thinks of it as a positive signal (Smith and Watts, 1992). The greater the reaction to a signal that reflects the expectation of market participants will result in a large amount of asymmetric information.

THEORETICAL REVIEW

Investment Opportunity Set

Investment opportunity sets play an important role in the company's financial theory. Since the combined asset in place with investment opportunities will affect the capital structure, dividend policy as well as on the performance of the Company. (Smith and Watts, 1992). The company will not grow



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or have grown in shares that only because of having assets and profits that increase over time. This is because the core of growth is not expansion, but the existence of a company's opportunity to invest large sums of funds with greater returns than normal returns on the stock market. Investment opportunity sets according to Myers and Majluf (1984), can be understood as management of signaling theory to outsiders. Set investment opportunities based on theoretical and empirical articles. In general, can be interpreted as the future growth prospects of the company seen from the investor's point of view and other external parties. Companies that issue shares, generally to raise the amount of cash in taking investment opportunities. Management is considered to know more about the value of the company than the potential investors. Investors interpret corporate actions as rational. The decision balance model for investment is developed with all these assumptions. The investment balance model shows that firms can refuse to issue shares and can miss important investment opportunities. The investment equilibrium model provides an explanation of some aspects of corporate financing behavior, which include trends that depend on internal funding sources and choose debt when external financing is required. Thus, the rule of thumb is to take every positive project of the NPV (net present value), both internal and external funds are used to pay it.

Companies that have high investment opportunity sets, will generally provide high performance targets for the executive accompanied by large reward bonuses if the target is achievable. Kallapur and Trombley (1999, 2001), inventoried and categorized measurement of investment opportunity sets commonly used in empirical research. There are several proxies used to measure investment opportunity sets that are grouped into price-based proxies, investment-based proxies, and variance-based proxies. (Kallapur and Trombley, 2001). Of the three proxies with several sections within each proxy, this study takes 3 (three) variables from various proxies, ie Market to Book Value of Equity (MBE) This ratio reflects that the market return value of the company's investment in the period will come will be greater than expected return from equity. Companies that have high MBE ratios will have the large

asset and equity growth, so that will be positively correlated. The formula used to calculate the market to book value of equity is $MBE = (\text{Number of Shares Circulated} \times \text{Stock Price Closing}) / \text{Total Equity}$, Ratio of Depreciation to Firm Value (DEP) This ratio shows the amount of reduction in assets in place. According to Smith and Watts (1992), the greater the DEP ratio indicates the investment opportunity of this ratio using the formula $DEP = \text{Depreciation Cost} / \text{Total Assets} - \text{Total Equity} + (\text{Stock Price Circular} \times \text{Stock Closing Price})$ and Ratio of capital expenditure to book value of assets (CAPBVA) this ratio indicates the existence of additional capital flows of the company based on book value of assets. This ratio can be calculated using the formula:

The book value of fixed assets t -

$$CAPBVA = \frac{\text{The book value of fixed assets at } t-1}{\text{Total assets}_t}$$

Company performance

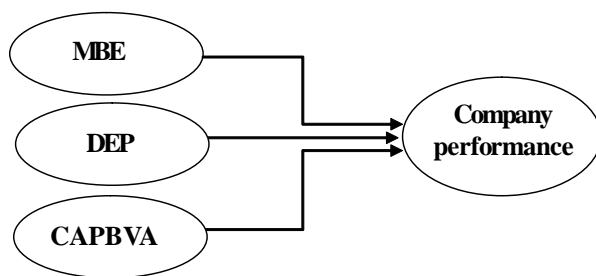
Performance comes from the notion of performance. There is also a definition of performance as a result of work or work performance. However, in fact, performance has a broader meaning, not only the work but also included during the work process (Winarno, 2003). This study uses two approaches to measuring company performance that is the accounting approach (Financial Performance) and Market approach (Firm Value).

Financial Performance

Financial Performance is something generated by the company within a certain period with reference to the standard set. Financial Performance should be measurable and describe the empirical condition of an enterprise of any agreed size. Understanding Financial Performance is an analysis conducted to see how far a company has implemented by using the rules of financial implementation properly and correctly. Such as making a financial statement that has met the standards and provisions in IFRS (GAAP) or GAAP (General Accepted Accounting Principle), and others.

Firm Value

Firm Value according to Wikipedia is an economic measure that reflects the market value of all businesses. It is intended that the number of claims of all holders of securities, debt holders, priority shareholders, minority interests, common shareholders, and others. Firm value is one of the basic metrics used in business valuation, financial modeling, accounting and portfolio analysis. A Firm value is equal to the Present Value of the company or in other words, equals the addition of separate asset values. Company performance in this study is measured using profitability performance Return on Investment (ROI) is a comparison between profit and all assets with the aim of assessing the best alternative use of capital or direct management attention on the implementation of the business as a whole. The research model can be described as follows.



Research methodology

Types of research

This research belongs to explanatory research because this research is done to explain the influence of Investment Opportunity to Company’s financial performance. In addition, the reason for choosing this type of research is to test the proposed hypothesis. It is expected through the hypothesis can be explained the influence of independent variables on the dependent variable.

Hypothesis

Preparation of research hypothesis refers to preliminary descriptions and theoretical reviews, then composed 4 (four) research hypothesis as follows. H1: Market to Book Value of Equity, Ratio of De-

- preciation to Firm Value, Ratio of capital expenditure to book value of assets simultaneously have an effect on Return On Investment (ROI).
- H2: Market to Book Value of Equity is partially significant to Return On Investment (ROI).
- H3: Ratio of Depreciation to Firm Value is partially significant to Return On Investment (ROI).
- H4: The ratio of capital expenditure to book value of assets is partially significant to Return On Investment (ROI).

Population and Sample

The population in this research is the company of Textile and Garment Sub-Sector Manufacturing listed on BEI year 2010 - 2014. The sample in this research is taken by using purposive sampling method, that is sample determination technique with certain criterion or consideration and adjusted to the purpose or research problem. A total sample of 8 companies for 5 years is 40 pooling data.

Data Analysis

Data analysis used in the research consisted of three kinds, namely Financial ratio analysis, Descriptive statistical analysis and Inferential statistical analysis. The inferential statistical analysis used in accordance with problem formulation, research objectives, and hypotheses. The hypothesis of this research is Classic Assumption Test and Hypothesis test with multiple linear regression is a regression using the independent variable (X) more than one with one dependent variable (Y).

Research Instruments

The data used in this study is secondary data with data sources derived from the Indonesian Capital Market Directory (ICMD), Indonesian Stock Exchange (IDX) statistic, and financial statements contained in the annual report of the manufacturing company Sub Sector of Textiles and Garments listed on the Stock Exchange 2010 - 2014. Based on time dimension and time sequence, this research is cross-sectional and time series or panel data. Data were obtained by using data collection technique from www.idx.co.id. In this research, there are four variables studied, namely Market to Book Value of Eq-

uity, Ratio of Depreciation to Firm Value, Ratio of capital expenditure to book value of assets, and Return On Investment which is divided into three exogenous variables and one endogenous variable.

Analysis and Discussion

Coefficient of Determination Test

The amount of contribution of Market to Book Value of Equity (MBE), Depreciation to Firm Value (DEP) and Capital expenditure to book value of assets (CAPBVA) to Return on Investment (ROI) can be determined by determination coefficient (adj R²) of 0.422 or by 42.2%. This means that the diversity of return on investment (ROI) variables can be explained by Market to Book Value of Equity (MBE), Depreciation to Firm Value (DEP) and Capital expenditure to book value of assets (CAPBVA), to Return on Investment) of 42.2%, or in other words the contribution of Market to Book Value of Equity (MBE), Depreciation to Firm Value (DEP) and Capital expenditure to book value of assets (CAPBVA), to Return on Investment (ROI) of 42.2% While the rest of 57.8% is a contribution of other variables that are not discussed in this study.

Testing Significance

Simultaneous Significance Test

H1: Market to Book Value of Equity, Ratio of Depreciation to Firm Value, Ratio of capital expenditure to book value of assets simultaneously affect Return On Investment (ROI). Simultaneous significance tests are used to determine the effect of the market to book value of equity (MBE), depreciation to firm value (DEP) and capital expenditure to book value of assets (CAPBVA) to return on investment (ROI), as in Hypothesis 1. The test criteria states that if the probability < level of significance (α) then there is a significant influence simultaneously influence the proportion of market to book value of equity (MBE), depreciation to firm value (DEP), and capital expenditure to book value of assets (CAPBVA) return on investment (ROI). Testing of significance simultaneously yields Fcount = 10.499 with probability 0.000. The test results show the probability < level of significance ($\alpha = 5\%$). It

can be interpreted that there is a significant influence simultaneously (together) market to book value of equity (MBE), depreciation to firm value (DEP) and capital expenditure to book value of assets (CAPBVA) to return on investment (ROI).

Partial Significance Test

H2: Market to Book Value of Equity is partially significant to Return On Investment (ROI). Testing Hypothesis to 2 that is a partial test of significance of market to book value of equity (MBE), yield t value equal to 5,311 with probability equal to 0.000. The test results show the probability < level of significance ($\alpha = 5\%$), meaning that there is a significant market to book value of equity (MBE) effect to return on investment (ROI).

H3: Ratio of Depreciation to Firm Value is partially significant to Return On Investment (ROI). Testing The third hypothesis is the test of partial significance of the variable depreciation to firm value (DEP) produces a value of t arithmetic of 2.378 with a probability of 0.023. The test results show the probability < level of significance ($\alpha = 5\%$), meaning that there is a significant depreciation to firm value (DEP) influence on return on investment (ROI).

H4: The ratio of capital expenditure to book value of assets is partially significant to Return On Investment (ROI). Testing The fourth hypothesis that the partial significance test of capital expenditure to book value of assets (CAPBVA) variable yields t count of 2.401 with a probability of 0.022. The test results show the probability < level of significance ($\alpha = 5\%$), meaning that there is a significant influence of capital expenditure to book value of assets (CAPBVA) to Return on Investment (ROI).

The partial significance test of investment opportunity set variables significantly influences company performance. If the direction of influence is marked positive, then it can be interpreted that the increase in investment opportunity set will be able to improve the performance of the company. The results of this study support the results of previous research Hasnawati (2005), the results indicate that investment decisions have a positive effect on com-

pany performance. Research Ehie and Olibe (2010), shows the set of investment opportunities significantly affect the company’s performance.

The results of this study support agency theory, which states that should within the company there is a separation between the owner as a principal and management as an agent. The objective of management is to maximize shareholder value that can be met by realizing investment opportunity sets into real growth that ultimately can improve company performance (Ehie and Olibe, 2010). The results of this study also support Signalling Theory, this theory states that if there is a positive investment signal then investors will be interested to buy shares of the company, so the market value increases. Conversely, if the investment information is negative then the investor will choose to release the stock of a company. A high investment opportunity set will be a positive signal for the market that can ultimately improve the company’s performance.

Empirical Model of Linear Regression

The regression equation from the estimation result of linear regression analysis is:

$$ROI = \beta_0 + \beta_1 MBE + \beta_2 DEP + \beta_3 CAPBVA$$

$$ROI = -0.891 + 1.901 MBE + 0.619 DEP + 0.185 CAPBVA$$

The constant of -0.891 indicates that if the market to book value of equity (MBE), depreciation to firm value (DEP) and capital expenditure to book value of assets (CAPBVA) are constant, then the return on investment (ROI) change is -0.891 %. The coefficient of the market to book value of equity (MBE) of 1,901 indicates that market to book value of equity (MBE) has a positive effect on return on investment (ROI). This means an increase of 1% market to book value of equity (MBE) will increase the return on investment (ROI) of 1.901%. The depreciation to firm value (DEP) coefficient of 0.619 indicates that depreciation to firm value (DEP) has a positive effect on return on investment (ROI). It can be interpreted that the increase of 1% depreciation to firm value (DEP), then will increase re-

turn on investment (ROI) equal to 0,619%. The coefficient of capital expenditure to book value of assets (CAPBVA) of 0.185 indicates that capital expenditure to book value of assets (CAPBVA) has a positive effect on return on investment (ROI). This means an increase of 1% of capital expenditure to book value of assets (CAPBVA) will increase the return on investment (ROI) of 0.185%.

Dominant Influence

The dominant influence of independent variables on the dependent variable can be seen through the largest standardized coefficient. The estimation results shown in the above table can be seen that the variable that has the largest standardization coefficient is the market to book value of equity (MBE) of 1.90%. Thus the market to book value of equity (MBE) has the most dominant influence on Return on investment (ROI).

CONCLUSIONS AND SUGGESTION

Conclusion

The result of the research shows that the contribution of the market to book value of equity (MBE), depreciation to firm value (DEP), and capital expenditure to book value of assets (CAPBVA) simultaneously to return on investment (ROI) is 42.2%. Partially, market to book value of equity (MBE), depreciation to firm value (DEP) and capital expenditure to book value of assets (CAPBVA) variables have significant influence. Market to book value of equity (MBE) variables has the most dominant influence on return on investment (ROI).

Suggestion

Based on the results of the research conclusions, the following suggestions are proposed. The company should be able to make Investment Opportunity Set (investment opportunity with the best to be able to generate a return as expected from the investment. In addition, for a further research is suggested to add other variables besides variables that have been used in this research. Use of dependent variable that uses Market sizes like Tobin’s Q needs to be used to show different contributions.

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