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THE EFFECT OF EARNINGS CHARACTERISTICS ON FIRM MARKET VALUE (CLOSING STOCK PRICE): EVIDENCE FROM CONSUMER CYCLICALS COMPANIES (IDXCYCLIC) ON THE INDONESIA STOCK EXCHANGE

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Abstract:
This study aims to analyze the effect of Net Income, Cash Flow from Operations (CFO), and Total Accruals (TA) on firm market value, proxied by closing stock price, in consumer cyclicals companies (IDXCYCLIC) listed on the Indonesia Stock Exchange for 2016–2025. The study uses a quantitative approach of the causal associative type with secondary data and purposive sampling. Multiple linear regression combining dummy variables with continuous independent variables is applied to 660 observations, with Category 3 (CFO < NI and TA < NI) as the reference category. CFO has a positive and significant effect on firm market value and is the variable with the largest effect (Beta = 0.482). Net Income has a significant negative effect (B = −0.098). Firms with CFO > NI (D1) and firms with TA > NI (D2) have significantly lower market values than the reference category. Simultaneously, the variables significantly affect market value, with an Adjusted R^2 of 17.8%. This study tests Net Income, CFO, and TA in one integrated model in the cyclical sector, and shows that the Indonesian capital market appreciates operating cash flow more than accounting earnings.
Keywords: Earnings characteristics; Net income; Cash flow from operations; Total accruals; Firm market value

INTRODUCTION

The Indonesian capital market shows continuous development, reflected in the growth in the number of investors, listed companies, and the intensity of stock trading activity on the Indonesia Stock Exchange (IDX). By 2025, the number of capital market investors had exceeded 17 million Single Investor Identification (SID), which indicates the increasing interest of the public in equity-based investment instruments. This condition encourages investors to be

more careful in evaluating companies before making investment decisions. One indicator that is the main concern of investors is firm market value, because it reflects the market's perception of the company's performance and prospects in the future (Bui et al., 2023). Firm value can be calculated in several ways; one of them is company's stock market price (Thesing & Velte, 2021). The closing price of the stock will reflect the sum of investor judgments about the par of the stock that they own, and the closing price will be an indicator that represents the market's reaction to company information in a time period.

Investors intensely use information available to them in the stock valuation process, particularly information that comes from financial statements. When examining financial statements, one of the most looked at parts of the statement is the earnings, as it is assumed that it represents the performance of a firm, and that it forms the basis of forecasting the profit generating capacity of the firm. However, one has to be aware that net income does not necessarily reflect fully the economic condition of the firm as earnings are accrual-based. Net income is not necessarily the best indicator of performance, and can actually be quite limiting. Investors should not only consider the net income amounts, but also the source of the income.

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Cash Flow from Operations (CFO) indicates a company's ability to produce and consume cash in its operating activities and total accruals (TA) refer to the portion of earnings that is related to the timing mismatch between cash realization and accounting recognition. Net income, CFO and TA therefore act as three complementary parts which are indicative of the nature of company earnings.

In the Indonesian capital market, several unusual phenomena are found. When CFO is greater than net income, TA is negative, which can reflect aggressive income-decreasing accruals or earnings that contain many discretionary non-cash expenses. More worrying from the perspective of financial analysis is when the magnitude of TA exceeds net income itself, which fundamentally indicates that most or even all reported earnings are no more than accounting constructs (Ochiai & Nacher, 2022; Jansen, 2021; Baig et al., 2020). The consumer cyclicals sector (IDXCYCLIC) is a sector with high dynamics and volatility, because its products depend heavily on economic conditions and the purchasing power of the public (Kaczmarek et al., 2021). This makes the sector an appropriate context for evaluating the relationship between earnings characteristics and firm market value.

Previous studies on the effect of earnings components on firm market value still show significant inconsistency. Budagaga (2017) and Jansen (2021) found that net income and CFO have a significant positive effect on market value, whereas Walkshäusl (2020) and Phuong and Hung (2020) stated that under high information asymmetry net income often loses its predictive power over stock prices because it is contaminated by discretionary accruals. Most previous

studies test the accrual component separately or in cross-sectoral analysis, thus ignoring the unique characteristics of the consumer cyclicals sector. The research questions are: (1) whether Net Income affects firm market value; (2) whether CFO affects firm market value; (3) whether firm market value differs between firms in Category 1 (CFO > NI) and the reference category (CFO < NI and TA < NI); (4) whether it differs between firms in Category 2 (TA > NI) and the reference category; and (5) whether Net Income, CFO, and TA jointly affect firm market value in consumer cyclicals companies on the IDX for 2016–2025.

The results of this study are expected to contribute to the literature related to the relationship between Net Income, CFO and TA and its implications for firm market value in the Indonesian capital market. Practically, it provides input for investors, company management, academics, and regulators on earnings quality, so that investors are not easily deceived by superficial earnings figures.

H1: Net Income has a positive effect on firm market value in consumer cyclicals companies listed on the Indonesia Stock Exchange for 2016–2025.

H2: Cash Flow from Operations (CFO) has a positive effect on firm market value in consumer cyclicals companies listed on the Indonesia Stock Exchange for 2016–2025.

In Category 1, a company's CFO is greater than the reported net income, which results in negative total accruals. According to signalling theory, stronger operating cash flow than

accounting earnings can be considered a sign that the reported earnings are of good quality, so investors tend to give a better valuation. In Category 2, when total accruals are greater than net income, CFO is mathematically negative, so the reported earnings are not supported at all by cash from operating activities; investors may doubt the company's ability to sustain that performance (Ochiai & Nacher, 2022; Thesing & Velte, 2021; Walkshäusl, 2020).

H3: There is a positive difference in firm market value between companies with Category 1 earnings characteristics (CFO > NI) and the reference category.

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H4: There is a negative difference in firm market value between companies with Category 2 earnings characteristics (TA > NI) and the reference category.

H5: Net Income, Cash Flow from Operations (CFO), and Total Accruals (TA) jointly have a significant effect on firm market value in consumer cyclicals companies listed on the Indonesia Stock Exchange for 2016–2025.

METHOD

Research type, population, and sample

This study uses a quantitative approach with a causal associative type of research, used to determine the cause-and-effect relationship between the independent variables and the dependent variable (Creswell & Creswell, 2017). The population is all companies in the Consumer Cyclicals sector (IDXCYCLIC) listed on the IDX during 2016–2025. The period covers the stable economic period before the pandemic (2016–2019), the COVID-19 pandemic disruption (2020–2021), and the period of recovery (2022–2025). Purposive sampling is used with these criteria: (1) consumer cyclicals companies consistently listed on the IDX during 2016–2025; (2) companies that routinely publish complete annual financial statements audited by an independent auditor; (3) companies with complete data on Net Income, Cash Flow from Operations, Total Accruals, and year-end market data; (4) companies that did not experience delisting; and (5) financial data presented in Indonesian Rupiah.

The data used in this study is secondary data, which is data that has been obtained from the annual financial statements, cash flow statements, and data from the capital market, which can be accessed in public on IDX (http://www.idx.co.id) and from the companies' websites, by documentation method.

Variable definitions

The dependent variable is the firm market value (MV) which is proxied by the closing stock price (LnMV). Net Income (NI) is measured as natural log of net income (LnNI) and Cash Flow from Operations (CFO) as natural log of operating cash flow (LnCFO). Total Accruals is a derived variable, calculated as the difference between net income and operating cash flow (TA = NI − CFO). Three types of earnings characteristics are identified based on empirical relationship between NI, CFO and TA. Dummy D1 equals 1 if CFO > NI (Category 1) and 0 otherwise; dummy D2 equals 1 if TA > NI (Category 2), which mathematically means that CFO is negative, and 0 otherwise. Category 3 (CFO < NI and TA < NI), which represents the normative and healthy reporting condition, is the reference category and is not given a dummy variable, to avoid the dummy variable trap.

2.1. Data analysis technique

All data are analyzed using SPSS. The analysis begins with descriptive statistics and classical assumption tests: normality (Kolmogorov-Smirnov test on the residuals; significance > 0.05), heteroskedasticity (Glejser test; all significance values > 0.05), multicollinearity (Tolerance > 0.10 and VIF < 10), and autocorrelation (Durbin-Watson test). Multiple linear regression is then applied with the following model:

$$LnMV = a + \beta 1LnNI + \beta 2LnCFO + \beta 3D1 + \beta 4D2 + \varepsilon$$

The coefficient of determination (Adjusted R^2), the simultaneous significance test (F test), and the partial significance test (t test) are used to test the hypotheses at a significance level of $\alpha = 0.05$.

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3. Results and discussion

3.1. Descriptive statistics

Table 1 shows that the number of observations (N) is 660. Firm market value (LnMV) has an average of 6.0448 with a standard deviation of 1.4038. Net income (LnNI) has an average of 24.9317, while operating cash flow (LnCFO) has an average of 24.8530. The slightly larger average of LnNI than LnCFO shows that, in general, the accounting earnings of the sample companies slightly exceed their operating cash flow. All variables have a standard deviation smaller than the average, so the data do not spread too widely.

Table 1. Descriptive statistics

Variable	N	Min	Max	Mean	Std. Dev.
LnMV	660	1.9459	9.9641	6.0448	1.4038
LnNI	660	16.2134	29.6089	24.9317	1.9692
LnCFO	660	17.8586	29.4194	24.8530	2.2470

Source: Author's data processing (SPSS).

Table 2 shows that the majority of observations (68.9%) are in Category 1, the condition in which operating cash flow exceeds net income. Category 2, earnings supported by accruals (TA

> NI), covers 15.8% of observations, while the normative (reference) category is 15.3%. This finding strengthens the existence of an unusual phenomenon in the relationship between NI, CFO, and TA in the Indonesian capital market, which is the motivation of this study.

Table 2. Distribution of earnings characteristic categories

Category	Criteria	Frequency	Percentage
Category 1 (D1 = 1)	CFO > NI	455	68.9%
Category 2 (D2 = 1)	TA > NI	104	15.8%
Category 3 (reference)	CFO < NI and TA < NI	101	15.3%
Total		660	100%

Source: Author's data processing (SPSS).

3.2. Classical assumption tests

The residuals are normally distributed (Kolmogorov-Smirnov statistic 0.029; Asymp. Sig. 0.200 > 0.05). The initial Glejser test on the ordinary least squares model showed heteroskedasticity in D1 (sig. 0.014) and LnCFO (sig. 0.004); the model was therefore re-estimated using Weighted Least Squares (WLS), after which all independent variables have significance between 0.719 and 0.957, so the homoskedasticity assumption is met. All variables have Tolerance between 0.536 and 0.565 and VIF between 1.769 and 1.865, so the non-multicollinearity assumption is met. The Durbin-Watson value is 0.521, which indicates positive autocorrelation; however, autocorrelation is not corrected in this study because the data are pooled cross-section and time-series data with 660 observations from many companies, and the autocorrelation test is relevant only for pure time-series data (Baltagi, 2021).

3.3. Multiple linear regression results

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Table 3. Multiple linear regression results (dependent variable: LnMV)

Variable	B	Std. Error	Beta	t	Sig.
(Constant)	1.359	0.705		1.929	0.054
LnNI	−0.098	0.034	−0.138	−2.862	0.004
LnCFO	0.301	0.029	0.482	10.264	0.000
D1 (CFO > NI)	−0.364	0.145	−0.120	−2.503	0.013
D2 (TA > NI)	−0.625	0.185	−0.162	−3.388	0.001

Source: Author's data processing (SPSS). Adjusted R^2 = 0.178; F = 36.602 (Sig. 0.000).

The regression equation is LnMV = 1.359 − 0.098 LnNI + 0.301 LnCFO − 0.364 D1 − 0.625 D2 + ε. A 1% increase in net income decreases market value by 0.098%, while a 1% increase in operating cash flow increases market value by 0.301%, assuming other variables are constant.

Companies with CFO > NI have an LnMV 0.364 lower than Category 3 (about 30.5% lower), and companies with TA > NI have an LnMV 0.625 lower (about 46.5% lower).

3.4. Hypothesis testing

The R value of 0.427 shows a moderate relationship between the independent variables and market value. The Adjusted R^2 of 0.178 means that 17.8% of the variation in firm market value can be explained by LnNI, LnCFO, D1, and D2, while 82.2% is explained by other factors outside the model, such as firm size, capital structure, and macroeconomic conditions. The F value of 36.602 with a significance of 0.000 (< 0.05) shows that LnNI, LnCFO, and the earnings characteristics (D1 and D2) simultaneously have a significant effect on firm market value, so the model is feasible to use and H5 is supported. Table 4 summarizes the partial tests.

Table 4. Summary of hypothesis testing

Hypothesis	Coefficient	t	Sig.	Direction	Conclusion
H1: NI → MV (positive)	−0.098	−2.862	0.004	Negative	Significant; opposite direction
H2: CFO → MV (positive)	0.301	10.264	0.000	Positive	Supported
H3: D1 (CFO > NI) (positive)	−0.364	−2.503	0.013	Negative	Significant; opposite direction
H4: D2 (TA > NI) (negative)	−0.625	−3.388	0.001	Negative	Supported
H5: Simultaneous	F = 36.602		0.000		Supported

Source: Author's data processing (SPSS).

3.5. Discussion

Net income shows a significant effect (sig. 0.004 < 0.05) with a negative direction (B = −0.098). When operating cash flow is controlled, an increase in net income is accompanied by a decrease in market value. This finding indicates that investors do not simply accept accrual earnings; earnings without cash support are perceived to have lower quality and therefore are not rewarded by the market. It is in line with Mostafa and Dixon (2024), who found that cash flow

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becomes more important for valuation as accruals become extreme.

Operating cash flow has a positive and significant effect (sig. 0.000; B = 0.301) and is the variable with the largest effect (Beta = 0.482). Cash actually obtained through operating activities is seen by investors as a more reliable indicator of performance and of the capacity to pay dividends than accrual-based earnings. This result is in line with Albuquerque et al. (2023), who concluded that cash flow measures have a more significant influence on stock prices than profit or loss, and supports Wilson (1986) and Bernard and Stober (1989), who showed the separate information content of operating cash flow beyond accrual earnings.

The effect of D1 is significantly negative (sig. 0.013; B = −0.364), which means that the market value of companies with CFO exceeding NI is lower than the reference category. In general, CFO > NI is considered an indication of quality earnings, so the negative direction contradicts the theoretical expectation (H3). A possible explanation is that in many sample companies CFO

> NI describes low earnings or high non-cash expenses (such as depreciation), so investors do not give additional appreciation.

The effect of D2 is significantly negative (sig. 0.001; B = −0.625), making it the dummy with the largest effect. The market value of companies whose earnings are mostly supported by accruals is about 46.5% lower than the reference category. This is in line with Sloan (1996), who stated that earnings containing a high accrual component are less persistent than cash-supported earnings and therefore receive a lower valuation from the market. Overall, operating cash flow is more appreciated by the Indonesian capital market than accounting earnings, while accrual-based earnings characteristics or the condition of CFO > NI are not always seen positively by investors.

Conclusion

This study shows that Net Income, Cash Flow from Operations, and Total Accruals jointly have a significant effect on the market value of consumer cyclicals companies on the Indonesia Stock Exchange for 2016–2025. Operating cash flow has a positive effect and is the most dominant variable, net income has a significant negative effect, and companies with CFO > NI or TA > NI have lower market values than the reference category, with the lowest values in companies with accrual-dominant earnings. The model explains 17.8% of the variation in market value; other factors such as firm size, capital structure, and macroeconomic conditions should be considered in future research.

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