The Effect of Profitability and Leverage on Stock Returns in Banking Companies in Indonesia

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ARTICLE INFO

Jurnal Economic Resources

ISSN: 2620-6196
Vol. 5 Issues 2 (2022)

Article history:
Received – August 23, 2022
Revised – September 16, 2022
Accepted – September 30, 2022

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Keywords:
Profitability (ROE)
Leverage (DER)
Stock Return

ABSTRACT

This study analyzes the Effect of Profitability and Leverage on Stock Returns in Banking Companies Listed on the Indonesia Stock Exchange. The population used in this study were banking companies listed on the Indonesia Stock Exchange during 2013-2017, totaling eight companies. The type of data used is secondary data originating from the publication of annual reports of Banking Companies Listed on the Indonesia Stock Exchange for the 2013-2017 period. The analysis technique uses multiple linear regression analysis. The results showed that only the Return on Equity variable partially had a positive and significant effect on stock returns with an ROE value of less than 0.05. Meanwhile, the Debt-to-Equity Ratio variable negatively and significantly affects stock returns with a DER value of less than 0.05. The coefficient of determination shows a value of 0.634. This means that 63.4% of Return on Equity (ROE) is explained by the Profitability and Debt To Equity (DER) variables or Leverage variables. The remaining 36.6% is influenced by other factors not included in this research model..

INTRODUCTION

In principle, the capital market is a means of meeting those who need capital with the owners of capital (Hajering & Muslim, 2022). Individuals and groups with various types of securities offer different levels of return with other risks. The capital market has two functions, namely, the economic and financial functions (Ahmad et al., 2018; Arsyad et al., 2021). To carry out its economic position, the capital market can channel funds effectively from owners of capital to those in need. At the same time, the financial function means that the capital market is a place to improve the welfare of capital owners through profit sharing (dividends), which is compensation for the funds invested in obtaining returns. The capital market is an activity related to public offerings and securities trading, public companies related to the protection they issue, and institutions and professions related to securities. The capital market provides a variety of other investment alternatives, such as: saving at the bank, buying gold, insurance, land, buildings, and so on. The capital market acts as a liaison between investors and companies or government institutions through long-term trading of instruments such as bonds, stocks, and others (Amin et al., 2021).

Return is the excess of the selling price of the shares from the purchase price, generally expressed as a percentage of the purchase proceeds. The higher the stock's selling price above the purchase price, the higher the return investors receive. Stock returns can be positive or negative. If it is positive, it means you get Capital Gain, whereas if it is negative, it means you lose or get Capital Lost. As rational individuals, investors will consider the amount of return that will be received with the amount of risk that must be borne as a consequence of the decisions that have been taken in investing. Investors who buy stocks have the hope of obtaining high returns while investing. However, if an investor wants a high rate of return, the risk that must be accepted is also high; conversely, if an investor wants a low rate of return, the chance that will be borne is also common. Therefore, an effective investment plan is essential to maintain their investment. Therefore, analysis and prediction of a company's financial condition are critical. Profit is the primary goal of every company in running a business. The greater the profit earned by a company, the better the company's performance. Because company profits can affect the development of a company's survival, these goals sometimes need to be adequately realized because companies often face problems and challenges that cause companies to experience activities.

Financial statements are generally prepared to provide information regarding the financial position. Performance and changes in the financial part of a company that is beneficial to interested parties, both internal to the company and external parties in making this decision, are essential things that must be done as well as possible to determine the performance to be achieved by the company. To assess the company's financial performance, it is necessary to calculate financial ratios, where ratios often used are profitability, solvency, liquidity, leverage, activity, profitability, and many other ratios that can be used to assess a company's financial performance. However, this study focused on profitability ratios and leverage ratios.

Profitability is the ability to earn profits or gains and a percentage measure used to assess the extent to which a company can generate current and future profits. Profitability is a company's ability to operate long-term depending on a decent profit. Profitability is the net result of several policies and decisions chosen by the management of an organization. Profitability ratios indicate how effectively the overall company is managed. While the leverage ratio is a ratio used to measure how much of a company's assets come from debt or capital, with this ratio, it can be seen the position of the company and its fixed obligations to other parties, as well as the balance of the value of fixed assets with existing capital. Leverage aims to measure the extent to which the company's financial needs are financed with borrowed funds.

The research object is banking companies listed on the Indonesia Stock Exchange. In contrast, an industrial company needs to pay attention to obligations that must be fulfilled immediately; besides that, companies need to pay attention so that they can use their assets or funds to gain profits or income from banking activities conducted. The problem that occurs in the company is that the profitability or profit has decreased, so with a decrease in company profitability, it is necessary to examine the relationship between profitability and leverage in relation to stock returns or the results obtained from investments made.

Financial statement analysis is closely related to the field of accounting. Accounting activities are recording, analyzing, presenting, and interpreting financial data from corporate institutions and other institutions where activities are related to the production and exchange of goods or services (Fuadah & Setiyawati, 2020). For an institution that aims to make a profit. Accounting provides a method for determining whether the institution gains or incurs a loss due to the transactions it undertakes. Accounting can provide information about the condition of the company and the company's operating results as reflected in the financial statements of the company concerned (Montoya, 2018). Therefore accounting (financial reports) can be used to communicate with parties interested in the company's financial data.

The financial condition and operating results of the company reflected in the company's financial reports are the final result of the accounting activities of the company concerned. Information about the company's financial condition and operating results are beneficial for various parties within and outside the company (Young et al., 2018). This helpful information, for example, is about the company's ability to pay off short-term and short-term debt, the company's ability to pay interest and loan principal, and the company's success in increasing the amount of its capital. Financial reports are general (Umar et al., 2019). The report is intended for various parties who have different interests. Investors or owners or investments (in a company in the form of a company are called shareholders) have an interest in knowing the potential for capital invested in the company to generate income (revenue received by shareholders is dividends) (Bahri & Komarudin, 2019).

Creditors have an interest in granting loans to companies, and the government (especially tax agencies) has an interest in determining the tax burden to be paid by companies. For investors and creditors, financial reports provide relevant information (historically and quantitatively) regarding changes in financial position and the company's ability to generate profits (Bahri & Komarudin, 2019). Apart from these three parties, there are other users of financial reports, namely employees, customers, and the public, who are interested in information on the stability and profitability of the company. Customers are concerned with the survival of the company. The community needs information about trends and the latest developments in companies' prosperity and activities (Young et al., 2018).

Financial statements (financial statements) are the final product and a series of processes for recording and summarizing business transaction data (Montoya, 2018). Arief Sugiro and Edi Untung (2016: 3) financial statements are the result of accounting activities (accounting cycle) that reflect the company's financial condition and operating results. Financial reports are a variety of information that users use to make decisions. Financial reports are an essential tool for obtaining information regarding the financial position and operating results that have been achieved by the company concerned. This information can be used as a basis for making economic decisions by management and external parties (Young et al., 2018). Decisions taken by users of financial statements can be in the form of investment decisions, lending, or management in processing companies to increase the efficiency and effectiveness of their operations.

During a severe economic crisis, a company is forced to stop its operations (Sudana, 2019). The consideration is the rising price of raw materials and other supporting materials. If the selling price of the company's product is calculated, it cannot cover the increase in costs incurred by the company. The company finally had to make a breakthrough in order to be able to maintain its debt to the debtor (the creditor). Actions taken by the company included diverting available funds to agencies that were more profitable at the time, namely buying dollars. When the price was high, the company sold them to get large rupiah profits (Iskandar, 2019). In addition, the company also made improvements to its funds on the other side, paid off its maturing debts by first negotiating so that its value could be promoted with a new rupiah value and other activities which were essential to save the company from bankruptcy due to the economic crisis (Niati et al. al., 2019).

Stated that financial management can be interpreted as a whole activity related to efforts to obtain funds, use and allocate these funds. Financial Management is the result of summarizing the company's financial data (Dahlia & Lelawati, 2019). These financial statements have been prepared and interpreted for the benefit of management and other parties concerned or interested in the company's financial data. Financial management as financial management is the process of making decisions about assets and financing the asset and distributing all potential cash flows generated from the asset. Therefore, financial management involves three significant decisions affecting various departments in a hospitality organization (Indrawati, 2019).

Profitability is essential thing in our business. We want better profits with our efforts than borrowing from banks or opportunities obtained through low-risk interest payments. This is the method most commonly used to evaluate whether or not you are good at running a business (Dianitha et al., 2020). For example, if savings or the money market generates a greater return than the money invested in the company, you might consider selling your business investment in some way. This ratio will measure the profit from sales (return on sales), profit from assets (return on assets), and profit from investment (return on investment) (Arsita, 2020). Profitability, also known as income, is obtained from price, volume changes, or both. Therefore a change in the ratio that takes place over time will occur with the work done affecting the change in the price of a volume. This occurs when costs increase, such as adding a sales force, depreciating assets, adding something else, or borrowing occurs.

The most crucial ultimate goal that a company will achieve is to obtain maximum profits or profits besides other things (Sari & Indrarini, 2020). By obtaining maximum profits as targeted, the company can do much for the welfare of owners and employees, as well as improve product quality and make new investments. Therefore, in practice, company management is required to be able to meet the targets that have been set (Arnita & Aulia, 2020). This means that the amount of profit must be achieved as expected and does not mean the origin of the profit. To measure the profit level of a company, profit ratios or profitability ratios, also known as profitability ratios, are used; according to Fadhila & Christiana (2020), the profitability ratio is a ratio for assessing a company's ability to make a profit. This ratio also measures the activity level of a company's management. This is addressed by the profit generated from sales and investment income. The point is that using this ratio shows the company's efficiency. Prihadi (2010) in Sari & Indrarini (2020) argues that the profitability ratio is the primary measure of a company's success in obtaining profit (profit). From the definitions put forward, investors and creditors are interested in evaluating a company's ability to generate profits now and in the future. The profitability ratio consists of the margin ratio on sales, the ratio of return on total assets, known as the return on assets ratio, and the ratio of return on equity in standard stock or the return on equity ratio.

A company running its business in line with the development it is experiencing always requires additional capital (Dianitha et al., 2020). In an established company, the ordinary owner determines what sources of capital are used, whether all of them come from ordinary capital, or whether there is a need for long-term debt. Every decision taken about the source of capital always has an impact. For example, if the source of joint stock capital is an obligation to pay dividends, policy or management decisions from shareholders need to be considered. Suppose the source of capital is from preferred stock. In that case, there is an obligation to pay dividends which must be prioritized. In the company's obligation to liquidate, preferred shareholders will have priority to increase the value of their shares (Arsita, 2020). If the source of capital comes from long-term debt, there is an obligation to pay interest and repay the debt at maturity.

According to Syamsuddin (2011) in Sari & Indrarini (2020), Leverage shows the extent to which debt and preferred shares are used in the company's capital structure. The company's leverage will affect earnings per share, the risk level, and stock price. The value of companies that do not have debt for the first time will rise when the need for additional capital is met by debt, and this value will then reach its peak, and finally, the value will decrease after using excess debt. Leverage is the use of funds with a fixed burden with the hope that this use will increase earnings per share (Arnita & Aulia, 2020). The problem of financial leverage only arises after the company uses it and with fixed expenses, just as the problem of operating leverage arises after the company has fixed costs in its operations. Companies that use funds with fixed costs are said to produce favorable financial leverage or a positive effect if the income received from these funds is greater than the fixed costs from using these funds (Fadhila & Christiana, 2020).

Shares are securities issued by a company as a tool to increase long-term capital (Alstadsæter et al., 2017). Buyers of shares pay money to the company, and they receive a share certificate as proof of their ownership of the shares, and their ownership is recorded in the company's register of shares (Bawamenewi & Afriyeni, 2019). Shareholders of a company are legal owners and are entitled to receive a share of the profits earned by the company in the form of dividends. Shares are authentic certificates or signs that have the power for the holder to participate in the company, have a nominal value (currency), and can be traded (Pertiwi et al., 2016).

Representative ownership of a person in a limited liability company reflects the number of shares held. The more shares owned, the greater the degree of ownership. Shares are issued per unit form; therefore, each share is called a share (Puspitaningtyas et al., 2019). The shares issued by the company will later become proof of the shareholder's participation in the company. The amount accumulated in the company is called the share capital. Shares (Shares) are proof of ownership for investors or a sign of equity participation in companies that give rights to dividends and others according to the size of the paid-up capital (Rinnaya et al., 2016). Shares are proof of ownership or a sign of a person's participation in a particular company. Share ownership has rights in company ownership by showing the percentage of share ownership (Rinnaya et al., 2016).

Return is the result obtained from an investment. According to Alstadsæter et al. (2017), stock returns are divided into two: realized returns and expected returns. Realized return is a return that has occurred, calculated based on historical data. Return realization is essential in measuring company performance and as a basis for determining returns and risks in the future. The expected return is the expected return in the future and is still uncertain. In investing, investors are uncertain about the returns and risks they will face (Bawamenewi & Afriyeni, 2019). The greater the return expected to be obtained from an investment, the greater the risk, so it is said that the expected return has a positive relationship with risk. Higher risk is usually correlated with the opportunity to get a higher return, usually correlated with the opportunity to get a higher return. However, high returns do not always have to be accompanied by risky investments. This alone occurs in irrational markets (Pertiwi et al., 2016).

The returns received by investors in the capital market are divided into two types, namely current income (lancer income) and capital gains/capital losses (price difference profits) (Puspitaningtyas et al., 2019). Current income is the profit obtained through periodic payments such as dividends. These profits are usually received in cash or cash equivalents so that they can be cashed out quickly. For example, stock dividends are paid in the form of shares, usually converted into cash by selling the shares they receive (Alstadsæter et al., 2017). Meanwhile, capital gain (loss) is the difference in profit and loss experienced by shareholders because the current stock price is relatively higher or lower than the current stock price previously. If the current stock price (Pt) is higher than the previous period's stock price (Pt-1), then the shareholder experiences a capital gain (Rinnaya et al., 2016). If the opposite happens, the shareholders will experience a capital loss. The stock return used in this study is capital gain (loss). Capital gain (loss) is the difference in profit (loss) experienced by shareholders because the current stock price is relatively higher (lower) than the previous stock price.

H1. Profitability has a positive and significant effect on stock returns in banking companies listed on the Indonesia Stock ExchangeProfitability has a positive and significant effect on stock returns in banking companies listed on the Indonesia Stock Exchange

H2. Leverage has a negative and significant effect on stock returns in banking companies listed on the Indonesia Stock Exchange.

RESEARCH METHOD

This research was conducted at the Indonesia Stock Exchange by collecting data at the Indonesia Stock Exchange Representative Office. The population used in this study were banking companies listed on the Indonesia Stock Exchange from 2013-2017; as many as eight samples were taken using a purposive sampling method. The type of data used is quantitative data, namely data that includes documents in the form of numbers and other data that can support this writer. To complete the data used in this study, the authors obtained data from secondary data, namely data obtained through the collection of company documents, such as company financial report data and other data that can support this discussion. The data that has been collected will be analyzed through four stages of testing. The first stage is to perform descriptive statistical tests. The second stage is the classical assumption test which consists of a normality test, multicollinearity test, and heteroscedasticity test. The third stage will be proven through a simultaneous test of the coefficient of determination and a partial test.

Table 1. Operational Variables and Measurements

Variable	Indicator	Reference
Profitability	Return On Equity (ROE) = Profit after tax: Modal sendiri x 100%	(Dianitha et al., 2020)
Leverage	Debt To Equity Ratio (DER) = Total debt: Own capital x 100%	(Sari & Indrarini, 2020)
Stock Returns	Stock Returns = Pt-Pt-1: Pt-1 x 100%	(Bawamenewi & Afriyeni, 2019)

RESULTS AND DISCUSSION

Statistical descriptions are used to analyze data by describing or describing the data that has been collected as it is without intending to make general conclusions.

Table 2. Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
ROE X1	40	-.63	4.91	2.3842	1.45622
DER X2	40	.32	4.80	3.6825	.82854
Stock_Return	40	5.63	10.93	8.4872	1.72503
Valid N (listwise)	40				

Table 2 shows that the stock return variable with a total of 40 data (N) has an average stock return of 8,487 with a minimum stock price of 5.63 and a maximum of 10.93, with a standard deviation of 1.7276. The Return on Equity variable with a total of 40 data (N) has an average presentation of 2,384 with a minimum value of -63% and a maximum of 4.91%, with a standard deviation of 1.45622%. Variable Debt to Equity Ratio with a total of 40 data (N) has an average presentation of 3.682%, with a minimum value of .32% and a maximum of 4.80%, with a standard deviation of .82854%.

The normality test aims to test whether the dependent and independent variables in the regression model both have a normal distribution or not. Standard P-P plots and standardized regression have dots spread around the diagonal line, so it can prove that regression analysis can or is feasible to use even though the plot deviates a little from the diagonal line, as seen in Figure 1.

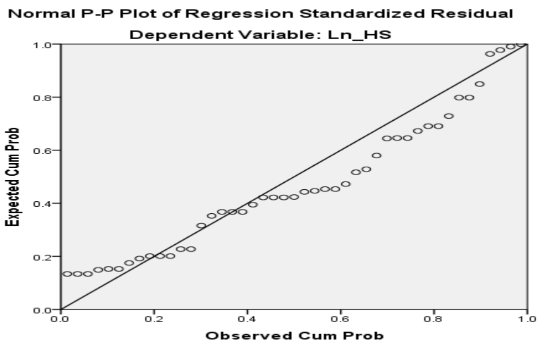

Figure 1. Data Normality Test Results

Furthermore, a multicollinearity test was carried out to determine whether there were deviations from the classical multicollinearity assumption, namely the existence of a linear relationship between the independent variables in the regression model. The test method used in this study is to look at the inflation factor (VIF) value in the regression model, according to Santoso (2001); for more details, see table 3.

Table 3. Multicholinearity Test Results

Model		Collinearity Statistics	
		Tolerance	VIF
	(Constant)		
1	ROE X1	.847	1.180
	DER X2	.847	1.180

Source: SPSS Appendix

From the results, the value of the variance inflation factor (VIF) of the three variables, namely ROE and DR, is less than 5, and the tolerance value is less than 1, so it can be concluded that between the independent variables, there is no multicollinearity problem. The Glejser test is carried out by regressing between the independent variables and their residual absolute values (ABS_RES). If the significance value between the independent variables and the absolute residual is more than 0.05, there is no heteroscedasticity problem.

Table 4. Heteroskedasticity test (Glesjer test)

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.072	.319		.226	.848
	ROE_X1	.069	.100	.115	.690	.521
	DER_X2	.143	.082	.309	1.744	.068

Source: SPSS Appendix

In table 4, the significance value of the three independent variables is more than 0.05. Thus, it can be concluded that there is no heteroscedasticity problem in the regression model. Multiple linear regression analysis in this study was used to determine the linear relationship between the independent variables on the dependent variable, whether each independent variable had a positive or negative effect, and to predict the value of the dependent variable if the independent variable experienced an increase or decrease.

This analysis determines the proportion of the variable contribution Return on Equity, Debt Ratio, to stock returns.

Table 5. Correlation Coefficient and Determinant Coefficient

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.824	.634	.610	1.24176

Source: SPSS Appendix

The correlation coefficient (R) = 0.824 indicates that the correlation of the independent variables (Return on Equity and Debt Ratio) with the dependent variable (stock returns) is very closely related and has a positive value, and is close to 1. The coefficient of determination (R2) = 0.634, which indicates that the variation of the price of shares (Y) in companies listed on the IDX can be explained by variables (Return on Equity, Debt Equity Ratio), amounting to 63.4%. In comparison, the remaining 36.6% is influenced by other factors.

Simultaneous testing is intended to determine how the independent variables consisting of the variables Return on Equity and the Debt Equity Ratio simultaneously (together) affect Stock Returns in Banking Companies Listed on the IDX.

Table 6. Simultaneous Test Results

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	64.195	2	32.098	23.191	.000[b]
	Residual	51.21	37	1.384		
	Total	115.405	39			

Source: SPSS Appendix

From the results of the ANOVA test or F-test, it is obtained that F-count =23.191 and a significance level of 0.000, less than 0.05, meaning that there is a significant influence between ROE and DER together (simultaneously) on stock returns at banking companies listed on the Indonesia Stock Exchange.

To determine the partial effect of each independent variable (Return on Equity, Debt Equity) on stock returns in Banking Companies Listed on the Indonesia Stock Exchange.

Table 7. Multiple Regression Analysis Results

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	9.229	0.862	0.000	10.706	.000
	ROE X1	0.957	0.152	0.819	6.296	.000
	DER X2	-0.796	0.257	-0.380	-3.097	.002

Source: SPSS Appendix

Suppose the company's Debt to Equity Ratio (DER) is high. In that case, the company's stock price will be low because if it earns profits, it tends to use those profits to pay its debts compared to dividing dividends. From the results of the regression analysis in table 7, the regression equation is obtained.

$$Y = \beta 0 + \beta 1X1 + \beta 2X2 + \beta 3X3 \text{ or } Y = 9.229X1 + 0.957\ X1 + -0.796\ X2.$$

The interpretation of the regression equation is as follows:

- β0 = 9,229, is a constant value, meaning that if the Return on Equity (X1) and the Debt Equity Ratio (X2) are fixed, then the stock return is IDR 9,229.
- β2 = 0.957 is the Return on Equity Coefficient Value (X1), meaning that if the Return On Equity variable increases by 1%, the stock return increases by IDR 0.957. The coefficient value is positive, meaning there is a positive relationship between Return on Equity (X1) and stock returns for companies listed on the IDX.
- β3 = -0.796 is the Debt Equity Ratio Coefficient Value (X2), meaning that if the independent variable Debt Equity Ratio (X2) increases by 1%, stock returns decrease by 0.796. The coefficient value is negative, meaning there is a negative relationship between the company's debt ratio (X1) and stock returns.

Discussion

The Effect of Profitability on Stock Returns

The results of testing the first hypothesis show that profitability proxied by ROE positively affects stock returns. These results indicate that when there is an increase in return on equity, it will increase stock returns. Meanwhile, judging from the partial test results, which show a significant influence between return on equity and stock returns, it can be concluded that an increase in return on equity will significantly affect an increase in stock returns, especially for banking companies listed on the Indonesia Stock Exchange. This is because a high ROE will be considered positive information. The higher the ROE indicates, the more efficiently the company uses its capital to generate profit or net profit for shareholders. The greater the ROE, the better the performance because the rate of return is more significant. With the increase in company performance, the share price of capital market companies increases, impacting stock returns so that the share of profits that occur with the rights of capital owners also increases. This study's results align with research conducted by Santoso (2010) examining the effect of ROA, ROE, and EPS on the stock returns of Go Public companies on the IDX in the food and beverage sector. The results showed that profitability, as measured by ROA and ROE, simultaneously influenced stock returns, while EPS also had a significant effect on stock returns. Meanwhile, Akroman (2010) research examined the effect of ROA, ROE, and EVA on stock returns listed on JII. The study's results show that ROA and ROE have a significant effect on stock returns, supporting the results of previous studies. The link between ROE and stock prices was put forward by Hinggins (1990: 59) in Sucitra (2010), explaining that there is a positive relationship between ROE and company stock prices which can increase the book value of company shares, so between ROE and stock prices have a positive relationship where ROE The higher the stock price, the higher the stock price tends to be. This will affect the stock return that the shareholders will receive.

Effect of Leverage on Stock Returns

The results of testing the first hypothesis show that leverage proxied by DER has a negative and significant effect on stock returns. These results indicate that any decrease in leverage proxied by DER will be followed by an increase in stock returns, especially in banking companies listed on the IDX. The higher the DER indicates, the higher the loan capital (debt) that the company uses to generate profits. As a result of this condition, the interest expense borne by the company becomes higher. The company's failure to pay interest or debt can cause financial difficulties, the latter in bankruptcy of the company. Increasing total liability (debt) shows a decreasing burden on the capital market. The company's stock returns also decrease with a decrease in stock prices. Research conducted by Thamrin (2012) examined the effect of the current ratio and DER on stock returns in manufacturing companies listed on the IDX. The results of this study indicate that the current ratio and DER partially affect stock returns is DER. In another study, Amran (2011) examined the effect of EPS, ROE, and DER on stock returns at JII companies in 2005-2007. The results of this study indicate that ROE has a positive effect on stock returns, while EPS and DER have no significant effect on stock returns. Then according to Robert Ang (2010: 18) explains the effect of DER that the higher the DER indicates the composition of the total debt (short term and long term) is greater than the total equity so that the impact on the company's burden on outsiders (creditors) is more significant. The increased burden on creditors shows that the company's capital sources are highly dependent on outsiders, reducing investors' interest in investing their funds in the company. The decline in investor interest has decreased the company's stock price, so the total return has decreased.

CONCLUSION

Profitability proxied by ROE positively and significantly affects stock returns in banking companies listed on the IDX. The analysis results and research that have been done show that leverage proxied by DER has a negative and significant effect on stock returns. It is recommended that investors investing in shares in banking companies on the Indonesian Stock Exchange should use the ROE and DER ratios. It is suggested that companies improve DER by reducing the amount of debt that has so far been owned by the company so that it can influence the increase in stock returns, especially in banking companies listed on the Indonesia Stock Exchange.

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