CHAPTER I
INTRODUCTION

1.1 Background of the Study

The key objective of the company financing decision is to maximize the wealth of the company (Mwangi, Makau, and Kosimbei, 2014). Financial decision making is very important for profitability. The company should know whether the return that they expect have been reached. To raise the profits, the company needs to expand their size. The company can buy new machines, opening new factory, making an investment, and those requires funds. Because the resources are scarce, the company should be wise in managing the resources.

The sources of long-term funding for business are divided into two categories, they are owner funding or known as equity, and borrowed funding or debt (Onyenwe and Glory, 2017). Equity funding means raising their fund by investor, they are owners of the company. The company issue shares to the investors who are willing to buy the company shares, the investor rewarded through the value of shares equity, and the dividend.

Debt financing means raising their fund by borrowing money from the bank. They are rewarded through interest payment, and the principal will be repaid according to the time specified in the agreement. The bank will take the company assets as collateral and have a first claim on the asset if the company failure to pay the debt.

The company should consider the alternative in financing decision that give more benefits to the company whether by using equity funding or debt financing. Debt financing or known as financial leverage is the use of debt for the purpose to get higher return from the investment. Financial leverage is important to show the financial analysis in view about trade-off between risk and potential return from the investment. The manager take charge in planning, analyzing, and controlling the operating activity of the company (Briliyan, Dwiatmanto, and Yaningwati, 2013).

The use of financial leverage in the company in hopes of increasing the return, and thus can give impact to the company income to increase, which also reflected the company earning per share to increase as well. On the other hand, the company needs to consider about the risk that may occur in using financial leverage, such as to pay the interest expense that affects the income of the company to decrease, in which can reflect the earning per share of the company to decrease as well. The existence of the high risk that may affect the investor behavior whether to invest or not, especially for the investors that are not a risktaker.

Earnings per share (EPS) is a financial measurement that indicates the profitability of the company. The importance of EPS makes financial managers achieve good corporate performance, especially in utilizing company capital and assets. Fluctuation of EPS influence by the changes of variables such as capital structure, and earnings before interest and taxes (EBIT), those are more concerned with alternative sources of debt funding or financial leverage (Maimunah and Rahajeng, 2015).

Factors affect EPS are the degree of financial leverage, debt to total asset ratio, and debt to equity ratio. The degree of financial leverage shows the percentage change in EPS to the percentage change in operating profit. If the degree of financial leverage increase indicates the EPS of the company to increase as well. Debt to total asset ratio indicates the proportion of the use of total debt to the total asset of the company. In order to be safe, total debt should not exceed the total asset of the company. Debt to equity ratio indicates a proportion of total debt to total shareholders' equity, to be safe, total shareholders' equity should exceed the total debt or at least the same (Briliyan, Dwiatmanto, and Yaningwati, 2013).

Other factors that affect EPS are return on equity, net sales, current ratio, inventory turnover, total asset turnover, net profit margin (Sutejo, Swasto, and Salim, 2010). Those variables affect EPS. This research will study the degree of financial leverage, debt to total asset ratio, and debt to equity ratio, which affect EPS.

Sub-sector textile and garment companies are classified as risky in their funding sources. Sources of funds in the sector are generally obtained from the banking sector, from the results of financing sources in the textile and garment companies, it is noted that the company uses great amount of debt which exceed the total asset, the use of large debt can cause the interest expenses to be large, if the total revenue is less than the company's expense, the risk of loss will be experienced by the company.

Table 1.1 Financial Data of Sub-Sector Textile and Garment Companies

Companies	Years	Total Asset (In million rupiah)	Total Liabilities (In million rupiah)	Total Revenue (In million rupiah)	Net Loss (In million rupiah)	Loss Per Share (IDR)
PT Argo Pantes Tbk.	2014	1,813,547	2,083,438	1,303,532	-377,232	-1,124.20
	2015	1,909,100	2,372,943	663,435	-159,947	-476.66
	2016	1,560,693	2,326,427	653,928	-345,536	-1,029.74
	2017	1,333,934	2,313,401	451,405	-201,484	-600.44
PT Asia Pacific Investama Tbk.	2014	2,041,304	2,310,084	2,129,058	-158,271	-48.82
	2015	1,944,326	2,512,252	1,891,190	-263,871	-81.25
	2016	1,619,757	2,544,730	1,296,753	-356,491	-109.79
	2017	3,458,737	3,109,652	1,640,409	-286,485	-91.88

Source: Financial data of Argo Pantes Tbk., and Asia Pacific Investama Tbk., from IDX.

PT Argo Pantes Tbk and PT Asia Pacific Investama Tbk are sub-sector textile and garment companies listed in Indonesia Stock Exchanges. According to the table 1.1 PT Argo Pantes Tbk in the year 2014 to 2017 respectively the total liabilities exceed the company total assets, and indicated this company used large amount of debt to operate the business. According to the data the total revenue in the year 2014 to 2017 decreased rapidly. In the year 2014 the total revenue was 1,303,532, the total revenue in 2015 was 663,435, in the year 2016 the total revenue was 653,928, and in the year 2017, the total revenue showed 451,405. The net loss reflects to the loss per share well.

According to table 1.1 above, showed the net income of PT Argo Pantes Tbk have negative results which are loss periodically from 2014 to 2017, in the year 2014 was -377,232, in 2015 the loss decreased to -159,947, in 2016 the loss increased to -345,536, and in 2017 the loss decreased to -201,484. The EPS in the year 2014 until 2017 result negative number which indicated loss periodically, during the year 2014 the loss per share showed -1,124.20, in 2015 the loss per share decreased to -476.66, in the year 2016 the loss per share increased to -1,029.74, in the year 2017 the loss per share decreased to -600.44.

According to the table 1.1 above, PT Asia Pacific Investama Tbk showed the total liability during 2014 to 2016 exceed the total asset, and indicated that this company use large amount of debt to operate. Where the total revenue during the year 2014 to 2016 decreased rapidly. In the year 2014 the total revenue showed 2,129,058, in 2015 was 1,891,190, and in 2016 was 1,296,753, while in the year 2017 the total revenue increased to 1,640,409.

According to the data above showed the problem of PT Asia Pacific Investama Tbk indicated loss during the year 2014 to 2016 respectively. In the year 2014 the net loss was -158,271, in the year 2015 was -263,871, in the year 2016 was -356,491, during 2017 the loss decreased to -286,485. Loss in the company reflects to the loss per share as well. The loss per share during the year 2014 to 2016 increased rapidly. In the year 2014 the loss per share was -48.82, in the year 2015 the was -81.25, in the year 2016 the was -109.79, while in the year 2017 decreased to -91.88. The data collected in accordance with the data in IDX of financial data of PT Asia Pacific Investama Tbk.

The use of debt which is too high result in the risk of financial distress. However, the use of financial leverage can be beneficial for tax payment, where it can help the company for tax saving. Besides, the use of financial leverage can increase the expected return of the company, the income of the company can increase by using the financial leverage optimally, increase in the income of the company will increase the EPS as well.

Based on the above of the background of the study, the writer comes out with this title **"The Impact of Financial Leverage on Earning Per Share on Sub-Sector of Textile and Garment Companies Listed in Indonesia Stock Exchange".**

1.2 Problem Limitation

This research will study about the impact of financial leverage on earning per share by considering variables such as return on equity, net sales, current ratio, inventory turnover, total asset turnover, net profit margin, degree of financial leverage, debt to total asset ratio, debt to equity ratio that affect EPS. Due to time constraints, the writer limits the variables. The variable used by writer is financial leverage that measure the degree of financial leverage, debt to total asset ratio, debt to equity ratio. This study focuses on how the financial leverage quoted sub-sector of textile and garment affects the earning per share.

1.3 Problem Formulation

Based on the background of the study, the problem in this study are as follows:

1. Does the Degree of Financial Leverage Partially affect on Earning Per Share in sub-sector textile and garment companies listed in IDX years period 2014-2018?
2. Does the Debt to Total Asset Ratio partially affect on Earning Per Share in sub-sector textile and garment companies listed in IDX years period 2014-2018?
3. Does the Debt to Equity Ratio Partially affect on Earning Per Share in sub-sector textile and garment companies listed in IDX years period 2014-2018?
4. Do the Degree of Financial Leverage, Debt to Total Asset Ratio, and Debt to Equity Ratio Simultaneously affect on Earning Per Share in sub-sector textile and garment companies listed in IDX years period 2014-2018?

1.4 Objective of the Research

The objectives of this study are to investigate the impact of financial leverage on earning per share in sub-sector textile and garment companies. The objective of the research are as follows:

1. To analyze the effect of the Degree of Financial Leverage partially on Earning Per Share in sub-sector textile and garment companies listed in IDX years period 2014-2018.
2. To analyze the effect of the Debt to Total Asset Ratio partially on Earning Per Share in sub-sector textile and garment companies listed in IDX years period 2014-2018.
3. To analyze the effect of the Debt to Equity Ratio Partially on Earning Per Share in sub-sector textile and garment companies listed in IDX years period 2014-2018.

4. To analyze the effect of the Degree of Financial Leverage, Debt to Total Asset Ratio, and Debt to Equity Ratio simultaneously on Earning Per Share in sub-sector textile and garment companies listed in IDX years period 2014-2018.

1.5 Benefit of the Research

The research is expected to give benefit both theoretically and practically

1.5.1 Theoretical Benefit

1. For Writer

This study is conducted for the writer to give better understanding about the impact of financial leverage on earning per share.

2. For Students

The result of this study is expected for the students to give information and contribution to the development of study especially in the field of financial leverage and earning per share.

3. For Academicians

This study of the research is expected to provide information and contribution to the development of study especially in the financial accounting in the field of corporate finance about financial leverage, besides the academicians can be use this research as reference or guideline for their future research, and comparison with previous research related to factors that affect the earning per share.

1.5.2 Practical Benefit

1. For Stakeholders of the Company

This study of the research is expected to give information to the financial user of the company. In order to have a better understanding regarding to the benefits and risk of using financial leverage, and to increase the financial performance of the company.

2. For Accounting Firm

This study is conducted to provide information to the accountant. In order to give a better understanding about the impact of financial leverage on earning per share, which can be apply in the real conditions.

1.6 Systems of Writing

System of writing in this research to provide a comprehensive picture of the contents of the study, in this research paper is divided into five chapters, there are:

CHAPTER I : INTRODUCTION

This chapter explain about the background of the study, and problem limitation. In this research, the problem formulation is formed from the problem in the background of the study. There is an objective of the study from the research that will be carried out. There is an explanation of the benefits of the study, and following with the system of writing.

CHAPTER II : LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT

This chapter is to provide theories which is the foundation of the study, the theories that will be support the formulation of the hypotheses. In this chapter is consist of theoretical background, previous research, hypothesis development, research model, and the framework of thinking.

CHAPTER III : RESEARCH METHODOLOGY

This chapter explain the methodology of the research. In this chapter consist of population and sample, followed by the definition of each variable used in the research, and method that will be used to collect the data and the data analysis.

CHAPTER IV : DATA ANALYSIS AND DISCUSSION

This chapter is to explain the research findings. In this chapter consist of the data classification, data analysis, descriptive statistic, the result of the data quality testing, the result of hypothesis testing and the discussion on this chapter.

CHAPTER V : CONCLUSION

This chapter consists of Conclusion, Implication, and Recommendation.