CHAPTER 1

INTRODUCTION

1.1. Background of the study

A company is an entity formed by a person, a group of individuals, or other entities to create and distribute goods and services to meet human economic needs. In general, businesses are formed to maximize profit while maintaining a specific level of shareholder welfare. This condition pushes financial management to be able to collect funds to meet the operational needs of the business in order to raise earnings and company value. The greater the company's value, the more prosperous the shareholders.

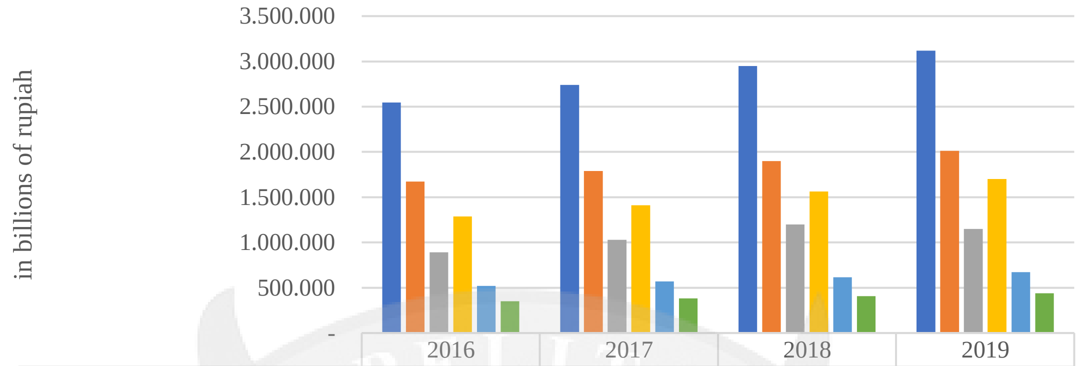
Every business, whether small or huge, has its own goals. The company can sustain its business continuity by increasing and maintaining its performance to compete in the market. One of the measures used in assessing a company's profit and performance is the profitability ratio, which is reflected in the theory of financial statements.

Financial statements provide insight into a company's financial performance. Ratios in financial statements can provide an overview of a company's financial health. Financial performance has an effect on the public's willingness to invest. Each entity that has gone public is also required to give accountability in the form of financial statements accessible to the public through the Indonesia Stock Exchange websites.

Food and beverage company is one of the manufacturing companies sector listed on the Indonesia Stock Exchange (IDX) and is a key contributor to Indonesia's economic development. It is critical to the nation's economic development. Food and beverage companies are businesses that manufacture things that meet basic human needs then sell products to earn a profit. Even in difficult economic times, the community requires the products. Thus, the food and beverage sector will stay stable and durable to the crisis compared to other industrial sectors. In other words, even in difficult or bad economic conditions, the community requires food and beverage. The food and beverage companies help a country absorb workers and increase income. In Indonesia, an increasing number of companies, both in the trade and service industries, are expanding rapidly.

The reason for choosing food and beverage companies as a research object is because food and beverage company is one of the manufacturing companies sectors that are classified as part of the consumer goods industry, which contributes significantly to Indonesia’s economic development, especially its contribution to the high growth in the gross domestic product (GDP).

The figure below shows the GDP from each industrial companies listed in Indonesia Stock Exchange for the year 2016-2019.



	2016	2017	2018	2019
Manufacturing	2.545.204	2.739.712	2.947.451	3.119.594
Agriculture, Forestry & Fishery	1.671.598	1.787.963	1.900.622	2.012.743
Mining & Quarrying	890.868	1.029.555	1.198.987	1.149.914
Construction	1.287.601	1.410.514	1.562.297	1.701.741
Financial & Insurance Services	520.207	571.204	616.315	671.434
Real Estate	350.488	382.259	406.014	439.456

Figure 1. 1 Contribution of the business sector to GDP (in billions of rupiah)

Sources: Indonesia Economic and Financial Statistics (2021)

Prepared by the researcher (2021)

As illustrated in Figure 1.1, manufacturing companies contribute a sizable portion of Indonesia's GDP. From 2016 to 2019, manufacturing companies' GDP continued to grow. From 2016 to 2017, the GDP increased by 7.64%. From 2017 to 2018, the GDP increased by 7.58%, while from 2018 to 2019, the GDP increased by 5.84%. The researcher focused on the food and beverage companies in this study.

The figure below shows the GDP contribution from the food and beverage companies listed in Indonesia Stock Exchange for the year 2016-2019.

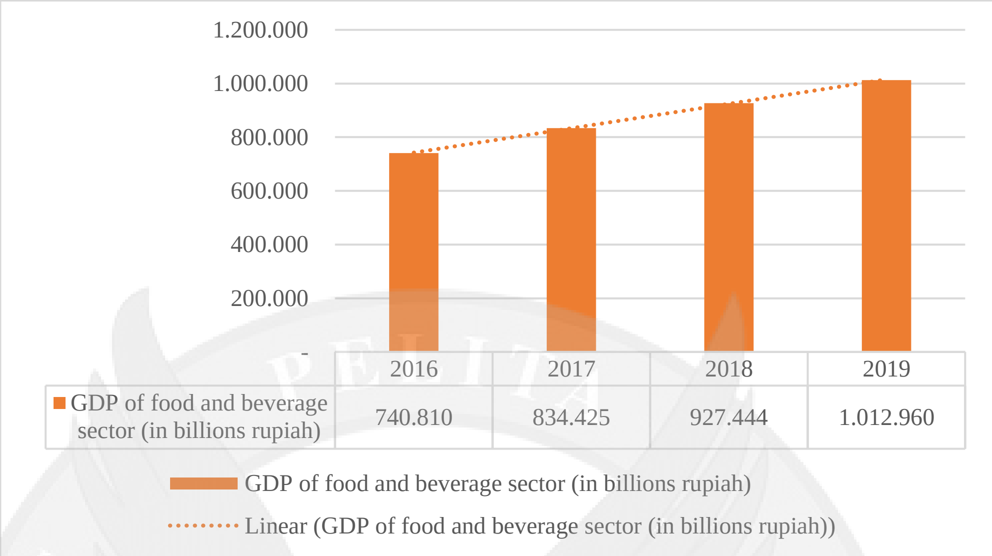


Figure 1. 2 GDP contribution of food and beverage sector (in billions of rupiah)

Source: Prepared by the researcher (2021)

As illustrated in figure 1.2, the food and beverage companies' GDP has always increased from 2016 to 2019. As can be seen, the GDP increased by 12.64% from 2016 to 2017, by 11.15% from 2017 to 2018, and by 9.22% from 2018 to 2019. Throughout the years examined, its performance accomplishments have been consistently positive, starting with its contribution to increased productivity, investment, exports, and employment. The increasing growth of the food and beverage companies is attributable to the Indonesian people's high level of consumption, where the community's need for basic daily needs such as food and beverage will always be required as one of the demands that must be met, which is followed up by the country's growing population as shown in figure 1.3. The increasing growth in food and beverage companies is projected to be able to support government programs in the food sector, particularly in the procurement of food of acceptable quality and nutritious content at accessible costs for the public.

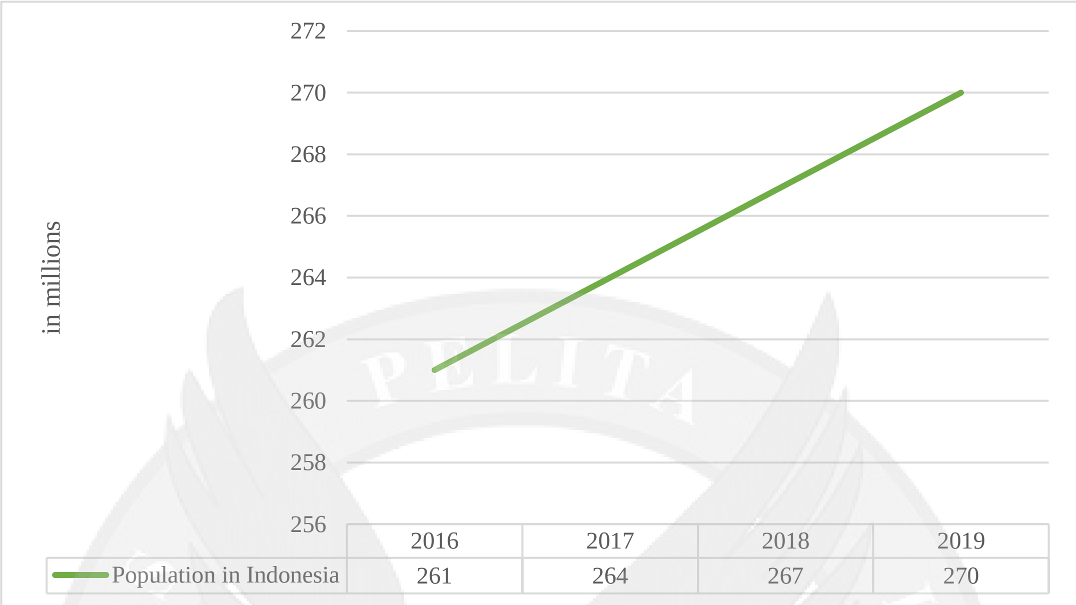


Figure 1. 3 Population growth in Indonesia

Sources: Prepared by the researcher (2021)

Profit maximization is one of a company's objectives. In achieving this goal, significantly competent management is required in order to optimize the company's profitability. The growth of food and beverage companies, it attracts investors and creditors interested in investing their assets. Investors must examine a company before choosing to invest by examining its financial performance to determine whether it has adopted strong management practices. Financial performance evaluation is essential due to the high level of risk and the quantity of money invested by investors. Investors can forecast a company's future prospects by looking at its financial performance and seeing how well the company manages and controls its resources in order to maximize earnings. Companies that perform well gain a competitive advantage that lasts. As a result, the company must continually be profitable in order for investors to remain interested in investing. The business will be able to continue operating if its profitability remains consistent. However, if the company's profitability is insufficient, it will be unable to sustain its operations.

Financial statement analysis can be used to evaluate a company’s performance. Financial ratios can be used to analyze financial statements. Ratios such as liquidity ratios, leverage ratios, activity ratios, market ratios, and profitability ratios are used to evaluate a company’s financial performance.

Profitability is the bottom line and primary goal of starting a business. Businesses that do not make a profit are unable to expand, pay employees, cover expenses, and meet other operating commitments. As a result, a lack of profit is the most telling sign that a company is having trouble, leading to bankruptcy and liquidation. Without profit, there may not be enough money to pay employees, cover operational costs, pay creditors, and meet other critical responsibilities shortly. As a result, investors, creditors, and financial institutions are especially interested in a company's profitability potential before deciding whether or not to participate in it, so rest certain that this area will be fully examined (Bhebhe, 2018, p. 18). Profitability refers to a company's ability to make a profit based on sales, total assets, and own capital. Profitability is important not only to business owners and managers but also to outsiders, particularly those having a relationship or interest in the company (Indriyani et al., 2017).

Return on Assets (ROA) was used as the profitability metric in this study. Return on assets is a profitability ratio used to determine a company's efficiency in generating profit from its total assets. It is one of the indicators used to determine a company's financial success. The ratio of net income after taxes to total assets is called the return on assets. The higher the return on assets, the better the performance of the business, as returns increase with time. (Iskarisma, 2017).

The use of debt in business activities also raises the leverage ratio. The debt-to-equity ratio was used in this study as the leverage ratio. The debt-to-equity ratio demonstrates the capacity of the company's own capital to finance debt. Additionally, the debt to equity ratio can provide an overview of a company's financial structure, allowing for assessing the risk of non-collectible debt. The smaller a company's debt-to-equity ratio, the greater the number of assets owned by the owner and the better the company's ability to meet its obligations (Indrawan, 2017).

The size of a business indicates its progress. The total value of a company's assets, sales, and market capitalization can all be used to assess its size. The more the total assets, sales, and market capitalization of the firm, the larger the firm. These three factors can be used to calculate the firm's size because they truly represent the firm's size (Azzahra & Nasib, 2019). As measured by total assets, firm size is more stable than firm size as measured by sales. This is because sales change more than total assets each year, whereas market capitalization value is the value of the firm computed by multiplying the number of outstanding shares by the market value of each share. Furthermore, companies with many total assets indicate that the company is a large company. Meanwhile, if the total assets owned are small, then the company is a small company. The increase of the total assets of a company demonstrates that it has more assets, giving confidence for investors to invest their money. Companies with big assets can maximize operational profits by utilizing available resources, whereas companies with minimal assets generate earnings that are in line with available resources (Chandra et al., 2021).

The ability of a company to use all its assets has an impact on its profit. To measure it, the researcher uses the total asset turnover. Total asset turnover measures how effectively a company's total asset is used to support sales. The faster a company's assets are turned over to support net sales operations, the more money it earns and the more profit it makes. The total asset turnover is a ratio that is calculated using sales proceeds to describe asset movements. Total asset turnover can be used to calculate the amount of capital invested in all rotating assets over a given time period, as well as the amount of money invested to earn money. The larger this ratio, the better because the company's assets can rotate faster to earn profits and generate sales due to the efficient use of assets (Chandra et al., 2021).

Table 1. 1 The Comparison of Debt-to-Equity Ratio, Firm Size, Total Asset Turnover and Return on Assets of Food and Beverage Companies listed in Indonesia Stock Exchange During 2016-2019

Company Name	Year	Debt to equity ratio	Firm size	Total asset turnover	Return on assets
INDF (PT. Indofood Sukses Makmur Tbk)	2016	0,87	32,04	0,81	0,06
	2017	0,88	32,11	0,79	0,06
	2018	0,93	32,20	0,76	0,05
	2019	0,77	32,20	0,80	0,06
ICBP (PT. Indofood CBP Sukses Makmur)	2016	0,56	30,99	1,19	0,13
	2017	0,56	31,08	1,13	0,11
	2018	0,51	31,17	1,12	0,14
	2019	0,45	31,29	1,09	0,14
MYOR (PT. Mayora Indah Tbk)	2016	1,06	30,19	1,42	0,18
	2017	1,03	30,33	1,40	0,11
	2018	1,06	30,50	1,37	0,10
	2019	0,92	30,58	1,31	0,11

Source: Prepared by the researcher (2021)

There are three food and beverage companies listed in Indonesia Stock Exchange that were chosen by the researcher, which are PT. Indofood Sukses Makmur Tbk, PT. Indofood CBP Sukses Makmur, and PT. Mayora Indah Tbk. The variable X_1 is represented by Debt-to-Equity Ratio, the variable X_2 is represented by Firm Size, the variable X_3 is represented by Total Asset Turnover, and the variable Y is represented by Return on Asset.

As shown on the table above, for PT. Mayora Indah Tbk (MYOR), the debt-to-equity ratio of the year 2016-2017 is decreased from 1.06 to 1.03. However, the return on assets is also decreasing from 0.18 to 0.11. Normally, when there is a decrease in the debt-to-equity ratio, the return on asset will increase.

This phenomenon also occurred in PT. Indofood Sukses Makmur Tbk (INDF), which INDF has the largest firm size, which means that INDF has the highest number of total assets compared to ICBP and MYOR. However, the return on assets is the lowest.

Another phenomenon also occurs in PT. Indofood CBP Sukses Makmur (ICBP), the total asset turnover of the year 2017-2018 is decrease from 1.13 to 1.12. However, the return on assets is increase from 0.11 to 0.14. Normally, when there is a decrease in total asset turnover, the return on asset will decrease.

Based on the information above, the researcher is interested in examining how debt to equity ratio, firm size, and total asset turnover influence the return on asset and write it in this research entitled "**The Influence of Debt to Equity Ratio,**

Firm Size and Total Asset Turnover toward Return on Assets on Food and Beverage Companies Listed in Indonesia Stock Exchange".

1.2. Problem Limitation

Based on the background of the study above, this research is going to be limited in:

1. The food and beverage companies within a period are 2016-2019.
2. This research data, such as financial reports, are obtained from Indonesia Stock Exchange (IDX).
3. The variables of this research were: Debt to Equity ratio (DER), Firm Size, Total Asset Turnover as independent variables, and Return on Asset as the dependent variable.

1.3. Problem Formulation

Based on the background and identification of the problems above, it can be concluded that this study has the following problem formulations:

1. Does debt to equity ratio have a significant influence toward return on assets on food and beverage companies listed in the Indonesia Stock Exchange for the year 2016-2019?
2. Does firm size have a significant influence toward return on assets on food and beverage companies listed in the Indonesia Stock Exchange for the year 2016-2019?

3. Does total asset turnover have a significant influence toward return on assets on food and beverage companies listed in the Indonesia Stock Exchange for the year 2016-2019?
4. Do debt to equity ratio, firm size, and total asset turnover have a significant influence toward return on assets on food and beverage companies listed in the Indonesia Stock Exchange for the year 2016-2019?

1.4. Objective of the research

In accordance with the problems that have been formulated previously with the subject then, the objectives of this research are:

1. To analyze the influence of debt to equity ratio towards return on assets on food and beverage companies listed in Indonesia Stock Exchange (IDX) for the year 2016-2019.
2. To analyze the influence of firm size towards return on assets on food and beverage companies listed in the Indonesia Stock Exchange (IDX) for the year 2016-2019.
3. To analyze the influence of total asset turnover towards return on assets on food and beverage companies listed in the Indonesia Stock Exchange (IDX) for the year 2016-2019.
4. To analyze the influence of debt to equity ratio, firm size, and total asset turnover towards return on assets on food and beverage companies listed in Indonesia Stock Exchange (IDX) for the year 2016-2019.

1.5. Benefit of the Research

1.5.1. Theoretical Benefit

Theoretically, the results of this research are expected to provide additional information and knowledge for academics regarding the influence of debt to equity, firm size, and total asset turnover towards return on asset. Besides that, the result of this research can also be used as a source of reading or reference that can provide theoretical and empirical information to those who will conduct further research on this issue and add existing literature sources.

1.5.2. Practical Benefit

The practical benefit of this research is as follows:

1. This research is designed to serve as a guideline for investors, managers, and creditors in order to assist them to improve the company's financial performance in terms of debt to equity ratio, firm size, total asset turnover, and return on assets.
2. As an additional reference that can be used as a comparison and contribute to other researchers who are interested in similar research. Useful in increasing knowledge and training yourself in solving problems scientifically in the economics fields, especially about financial analysis.

1.5.3. Researchers Benefit

For researchers, it is hoped that this research can be used as a practice thinking scientifically based on the discipline of knowledge obtained in university, making this research a reference for conducting further research.