CHAPTER 1

INTRODUCTION

1.1 Background of study

The manufacturing sector, which focuses on turning raw materials into a variety of goods, is one of the largest in Indonesia and is currently one of the fastest growing in the world. The Indonesian government closely monitors and supports this sector, with particularly significant implications for Indonesia's corporate sector, created substantial economic challenges as businesses faced sudden shifts in consumer behavior and widespread market uncertainty.

Understanding this impact is crucial as it not only exposed existing vulnerabilities within various industries but also revealed opportunities for businesses to develop greater resilience and adaptability. As companies were forced to rapidly transform their operations to survive, many discovered new pathways for growth and innovation, demonstrating the potential for positive change even in the face of severe economic disruption.

In 2023, Indonesia's manufacturing sector employed 19 million people, making it the largest employer in the country. Its large workforce and relatively low labor costs make the sector attractive for both domestic and foreign investment. This strong foundation positions Indonesia as a key player in the global manufacturing market.

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According to a report by the International Monetary Fund, Indonesia’s manufacturing sector demonstrated resilience, emerging as a key contributor to economic recovery. In the middle of 2021, the sector achieved a robust growth rate of 6.91%, significantly contributing 17.34% to the nation's GDP. Industries such as transportation equipment and basic metals were pivotal, with growth rates of 45.7% and 18.03% respectively. To support this momentum, the government provided targeted incentives like tax breaks and subsidized gas prices, which helped sustain production levels and strengthen domestic supply chain.

The government’s focus on enhancing local component use further reduced dependency on imports, reinforcing the sector's stability. Despite the broader economic pressures, the policies enabled manufacturers to maintain operations, adapt to changing market dynamics, and capitalize on increased demand in specific industries like chemicals and electronics. These strategic measures were crucial in allowing the manufacturing sector to drive economic growth and resilience in Indonesia. (Kementrian Perindustrian Republik Indonesia, 2021)

A company's overall financial health, as determined by financial analysis, is referred to as its financial performance. This assessment assists the business in pinpointing areas of achievement or possible problems over a given time frame, enabling management to make well-informed choices to improve performance and successfully handle obstacles.(Syafitri & Khalifaturofi’ah, 2023)

Although many factors can influence a company's financial performance, this research concentrating on five key variables such as liquidity, firm size, leverage, total asset turnover, and sales growth. By analyzing these factors, the research aims to highlight ways businesses can improve their performance and financial stability. This is especially important in today's uncertain economic climate, where understanding strengths and weaknesses can lead to better decision-making and help companies achieve long-term sustainability.

Table 1.1 Table of Phenomenon

Company	Year	Financial Performance (ROA)	Liquidity (CR)
MYOR	2020	0.0912	0.0361
	2021	0.0558	0.0233
	2022	0.0721	0.0262
	2023	0.1165	0.0367
AALI	2020	0.0390	0.0331
	2021	0.0658	0.0157
	2022	0.0512	0.0360
	2023	0.0359	0.0183

Source : Author (2024)

The table 1.1 illustrates the liquidity and financial performance of a sample of two manufacturing companies over a four years period (2020 to 2023). From the sample data, it is observed that both of the companies can be shown that there are eventually two do not exhibit distinct connection from both liquidity and financial performance, the table is provided to show the phenomenon that happens from all the data provided.

The two companies demonstrating a distinct correlation on both liquidity along with financial performance are MYOR and AALI. For AALI, despite fluctuating current ratios (CR) over the years, AALI showed an increase in financial performance from 3.9% to 6.5% during 2020 to 2021, which on the liquidity show opposite pattern from 3.3% to 1.5%.

On the same side, MYOR also clearly showing an inconsistent pattern for both liquidity and financial performance. From 2022 to 2023, MYOR's financial performance show a decline from 7.2% to 1.1%, yet its liquidity increase from 2.6% to 3.6%. Ideally, an increase in liquidity would correlate with improved financial performance, but in this case, the opposite occurred. This suggests that, for MYOR, higher liquidity did not translate to better financial outcomes, indicating that liquidity can be consider showing a negative or inconsistent affect on financial performance.

In proportion to the prior research, which was titled "The Effect Of Current Ratio, Total Asset Turnover And Debt To Equity Ratio On The Financial Performance Of Manufacturing Companies Listed On The Indonesia Stock Exchange For The 2015-2020 Period". The study mainly focuses not more than 12 companies on manufacturing sector that listed on the IDX 2015 until 2020. It focuses on analyzing how financial performance may impact liquidity, parallel with prior research by(Juliani et al., 2023). The result showing that liquidity positively impacting the financial performance, while higher current ratio (CR) was associated with increased liquidity and higher financial performance. This current study will adopt the same variables and analytical methods but will cover the period from 2020 to 2023. On the contrary, the prior research, which was titled " The Effect of Credit Risk, Capital Adequacy Ratio, Liquidity, Operational Efficiency, and Solvency on The Financial Performance The City of Denpasar".

The study is conducted with only 23 companies in 2018-2020, this research conclude that liquidity show insignificant impact on the financial performance.

The proposed study can contribute to more information from what already available on corporate finance in Indonesian context by concentrating on liquidity as the main variable and investigating its relationship to financial performance. It can also offer empirical data that guides business practices and decision-making. for this reasons the writer would conduct a thorough study that owns a title "**The Influence Of Liquidity Toward Financial Performance"**

1.2 Problem Formulation

Since the research only uses one primary variable, the entire research will ultimately concentrate on:

1. Does Liquidity has significant influence on Financial Performance?

1.3 Objective Of Research

Some objectives about this research as stated by the problem formulation stated above, are listed below:

1. To examine the significant influence of liquidity toward financial performance.

1.4 Benefit of the Research

The advantages about this research is stated below:

1.4.1 Theoretical Benefits

By offering a thorough research of the variables affecting financial performance in the manufacturing industry, this research adds to the information already in existence. It closes gaps in the literature about how financial leverage, sales growth, total asset turnover, firm size, along with liquidity and how the variable affect financial performance along with a thorough framework for comprehending the interactions between different financial measures and how they impact and effecting financial performance.

1.4.2 Practical Benefits

The research findings about the company financial performance of manufacturing firms listed on the IDX can be used by investors to help them make more well informed with capital allocation decisions. Investment plans and probability evaluations be might be influenced by knowing which factors have the most effects on financial performance.

1.5 Problem Limitation

1. The objects of this study fully focusing on manufacturing sector registered on Indonesia Stock Exchange.
2. The variables for this research contains one main variable which is liquidity, and four others control variable such as sales growth, financial leverage, company size, and total asset turnover all this variables stated are independent

variables, in addition of one more dependent variable which is financial performance.

3. The research data used in this paper starting from 2020-2023.