CHAPTER 1

INTRODUCTION

1.1 Background of Study

Public companies are called attractive to investors not only when their share prices are stable but also their ability to prepare their financial statements in a neat and credible manner is one of the plus points. Usually, investors would like a return in their investments. Although a rise in the share price after investing is a good way for investors to earn returns, if the company’s share price is unstable, it can make investors hesitant to buy or invest. In such cases, it's important to consider other factors like dividends. Dividend is another way for investors to earn their returns. Investors expect for the company to earn high profits; thus, those profits can be shared among investors in the shape of dividends.

When it comes to share prices, usually affected by the effect of offer and demand of the share and those effect will result in changes in share prices. Investors usually will purchase a share of a company if the price is low and in return expecting the payout when the share price increase to desired price, while owning the share of a company will result to investors earning dividends when the company is earning profit. At the end of the day, one must analyse the trend of company’s share price so that they will eventually have the right decision to either purchase or sell the share they owned (Tahan et al., 2023).

In this research paper non-cyclical companies will be the object of the research because of the nature of this sector, which generally provides essential goods and services that remain in demand regardless of economic conditions. Non-cyclical companies are often seen as more stable and less sensitive to economic fluctuations compared to cyclical sectors, making them a relevant focus for studying the relationship between profitability and share price. By examining this sector, the research aims to analyze whether financial performance indicators such as profitability continue to play a significant role in influencing stock prices even during periods of economic uncertainty.

The period of 2020 to 2024 was chosen because it captures a unique phase marked by significant global events, particularly the COVID-19 pandemic and the Russia-Ukraine war. The COVID-19 pandemic, which began in early 2020, brought severe disruptions to global markets, supply chains, and consumer behavior, creating a highly volatile economic environment. Following the pandemic, the Russia-Ukraine war that escalated in 2022 further contributed to global economic instability, particularly affecting energy prices, inflation, and market confidence. These events created an unusual context to observe how profitability affects share price under extreme global uncertainty. Studying this period provides valuable insights into how non-cyclical companies perform during crises and whether profitability remains a key factor influencing their stock valuation.

One of the ways to look at and analyse the company's performance is by looking at their profitability, how much profit will the company earn with the given assets in hand, company's main goal is to generate income or profit, some ways to measure profitability of a company is by using the ratio of Return On Asset (ROA), Return On Equity (ROE), etc. in a way investors would use this metric measurements in order for them to analyse the market. The trend for the share price to increase affected also by the profitability, with the profitability of a company increases the share price tend to increase more as well, and on the other hand, the share price would decrease when company's profitability also decreases (Tarihoran & Faris, 2024).

That shows in the evidence shown by the research done by (Sholichah et al., 2021), in which they stated that profitability has an influence in share price of a company, the relationship of profitability and share price has a positive relationship, which means when profitability of company increases in this case, return on asset the share price will also increase. But there is a difference with another research done by (Sahari & Suartana, 2020), which states that profitability in this case ROA in particular has no effect towards the share price of the company, because other factor such as merger, acquisition and government policy in a way could impact the price of the share of a company.

Company size can be one of the factors for investors to decide whether to invest into a company, company size can be measured in the terms of total assets, the amount of sales. Investors will try to decide whether to invest based on the size on the company itself. One might say size itself do not determine a company's good operation, but as humans, we tend to see the size of one thing. In this case, investors might see the amount of sales made by the company is a set period of time. If an investor decides that the company have made tons of sales in a certain amount of time, they might want to invest to the company, one cannot be stated so far when it comes to the total asset of the company, they might have seen the massive amount of assets of the company and decided that this is good enough to invest into them (Tahan et al., 2023). (Halawa et al., 2023).

Research done by (Tahan et al., 2023) stated that a company could attract investors to invest into their company if they are able to create or produce a good quality company. In this case, the size of the company, their total assets, or their sales. As such, according to the research, company size has impact towards the share price of a company. While the research made by (Sasongko Putra et al., 2024) stated that company size the case of total assets do not have significant affect towards the fluctuation of the stock prices.

Sales growth of a company can be affected by some factors such as the changes of sales price, the amount or volume of products being sold, etc. While a company can still sell their products in the same quantity, but by increasing the price, they will earn more revenue in general. Same thing if they sell in larger quantity with the same old price, they will still earn more revenue as before. Even though the revenue of a company increases, according to (Halawa et al., 2023), sales growth has no significant impact towards the company's share price. While on the other hand, (Nuridah et al., 2022) stated sales growth has significant effect towards the company's share price.

Liquidity is a part of a company performance. When it comes to liquidity, companies will have to handle them by being able to pay out their short-term debts. With that ability to pay out their debts, in this case creditors, companies that are not able to handle their liquidity, or in other words, companies that have low liquidity will be viewed as incapable of paying out to their creditors or other short-term debts. Therefore, it will be viewed by creditors that the management of the company is not capable of handling the situation. Thus, investors are more likely to invest into a company if they are deemed capable of paying out their creditors, as the investors also expected to receive dividends on time without any prolonged payment time. There are some ratios on calculating the liquidity, consist of current ratio, cash ratio, and quick ratio. For this research, current ratio will be used to measure the liquidity of the companies (Loya et al., 2022), (Tarihoran & Faris, 2024).

According to (Tarihoran & Faris, 2024), liquidity has a partial impact towards the company's share price positively, this means there is a small effect of the liquidity can influence the share price of the company. On the other hand, (Loya et al., 2022) stated that liquidity has partially no significant effect on the share price of the company, the statement means that liquidity have small to no effect on the share price of the company.

Leverage reflects a company's ability to meet both its long-term and short-term financial obligations. It is also linked to the company's profitability. The higher the level of leverage, the greater the trust the company gains from external parties. This indicates that if a company can borrow substantial funds, generate significant returns from those investments, and repay the borrowed money, it becomes an attractive proposition for investors looking to buy shares or invest in the company. (Bangun & Natsir, 2023). In this research, it will be concentrated in debt-to-equity ratio (DER).

According to (Salsabila et al., 2024), DER has significant effect towards the share price of the company, it is further stated that company's capital is usually better effect towards the share price if the capital is in large number. Not only that the success of the share price of the company benefits the owner, but also it benefits the shareholders of the company.

On the contrary, (Putri & Septiano, 2023) argued that DER has no significant effect towards the share price of a company. They explained that DER is not the only means of measurement indicates the increase or decrease of a share price but other factors also play in place such as the understanding of one investing into a company, understanding the comprehensive ways on how a company works or operate.

Thus, with the research gap that still happens in this research, along with the reasons explained above, the researcher is motivated to do research with the title "The Impact of Profitability towards Share Price of Consumer Non-Cyclical Companies", placing focus on Profitability as the main independent variable in this research, followed by controlling variables: Firm Size, Sales Growth, Liquidity, and Leverage, in order to further investigate the relationship between each variable.

1.2 Problem Formulation

The Problem Formulation regarding the background of study poses the following questions: Does profitability significantly affect the share price of Consumer Non-Cyclical companies?

1.3 Objectives of the Research

With the related problem formulation, thus, the objective of the research is to provide empirical proof, and show the effect of profitability towards share price of Consumer Non-Cyclical companies.

1.4 Benefits of the Research

This research is and will be expected to yield both theoretical and practical benefits, as listed below:

1.4.1 Theoretical Benefit

With this research, there is a hope that it could be used for future readers and future studies, the knowledge on how a company's profitability could affect their share price. With that in mind, there is a hope that this could be helpful for future researchers as references in order to help their research with a similar topic and would in a way create new and better research than this.

1.4.2 Practical Benefit

For the investors who would like to invest or purchase a company's shares, this research is anticipated to help them in deciding their purchase of company shares. It is also expected that this research could help them in understanding more on the strategy to gain returns on their end. For the company themselves, this research can offer them understanding that there are more factors to look at when it comes to their share price, and in this case, profitability is one of them.

1.5 Problem Limitation

The writer restricts the scope of the research to several problem limitations in order to prevent it from deviating from the discussion in question, limit the research coverage, and maintain effectiveness. Thus, this study uses one main independent variable, four control independent variables, and one dependent variable. Additionally, the firms analyzed in this study is limited only the Consumer Non-Cyclical companies registered on the Indonesia Stock Exchange within the period of five years, specifically 2020-2024.