

Proceedings of Annual Malaysia Business Research Conference

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Concorde Hotel Kuala Lumpur, Kuala Lumpur, Malaysia

Mr. Tanzil Hoque

**Global Research Institute for Business Academics
28 Harlington Street,
Clayton VIC 3168,
Melbourne, Australia**

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Editorial Note: These proceedings are organised under the following tracks:

**Accounting
Banking
Economics
Finance
Management
Marketing**

How to find your paper?

Papers contained in these proceedings are refereed papers as they are double blind peer reviewed. We have tried to minimise the errors but sole responsibility rests on the author(s) concerned. In some cases, we have provided "abstract" only as per instruction of the concerned author(s). We hope these papers would serve as the most valuable materials for business research only and no materials should be used or manipulated for any purpose other than purely academic research. We appreciate the contribution of the author(s) and our editorial staff who worked relentlessly to make the conference an outstanding success.

Mr. Tanzil Hoque

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Cash Flows, Debts dan Performance : Survey on the Cement and Ceramics Companies in 2010 – 2014

Rina Adi Kristianti* and Supinah**

This study tried to explore the effect of operating cash flow, investing cash flow, long term debt and short term debt on performance of cement and ceramics companies in 2010 – 2014. Selected samples are 45 companies and using panel data for analyzing them. The best method of panel data is pooled least square. R value is 0,237 and R square is 0,161. The result shows that long term debt has significant negative effect on performance. It proves that this industry is more likely to reduce the use of a debt to improve its performance. Funding chosen is internal fund namely retained earnings. This result supports pecking order hypothesis.

Keywords: performance, operational cash flow, investing cash flow, long term debt, short term debt, cement and ceramics industries.

1. Introduction

Indonesia economic conditions that had dropped starting with the declining Rupiah value, declining stock values, the case of large companies such as Ford, the government's plan to reduce staff. This indicates less favorable macro conditions in Indonesia. Nonetheless, the companies still grow particularly for infrastructure in various areas. The development of this infrastructure must be supported by other components such as the cement and ceramics industries. So this research is focusing on cement and ceramics industry because the industry is considered viable at this time.

Growth conducted by the firm of course requires a lot of capital. Capital can come from debt ie short and long-term debt. The use of debt can be beneficial if used optimally (trade-off theory, Modigliani and Miller,1958; Titman and Wessels, 1988, Rajin and Zingales, 1995) but it can also be detrimental if it raises financial cost and leads to

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bankruptcy so that better use of internal funds (pecking order theory, Myers et al, 1984 ; Asquith and Mullins, 1986) and Eckbo, 1986). Internal fund may come from the company's cash flow. The cash flow statement describes a statement of cash inflows and cash outflows of operating, investing and financing activities. We can utilize cash flow statement for the purpose of 1) assessing the company's ability to meet obligations, ability to pay dividends and the need for external financing, 2) assess the company's ability to generate net cash flows in the future. Therefore, funding both debt and cash flow will certainly give effect on performance. This study will explore the influence of operating cash flow, investing cash flow, short and long-term debt to the performance on the cement and ceramics companies.

2. Research Question

Do operating cash flow, investing cash flow, short term debt and long term debt have significant effect on performance?

3. Literature Review

Performance can be measured through financial and non-financial performance (Ittner, 2008). Among other non-financial performance can be measured by market share, degree of innovation, and customer satisfaction (Hyvonen, 2007). While financial measures can be seen through accounting measures such as return on assets, return on equity, EBIT, etc (Crabtree & DeBusk, 2008).

This study has four hypotheses are:

1) Cash flow and Performance

Effect of cash flow of the performance can be positive or negative. Cash flow has positive effect on performance because improving cash flow also increase company profit. Increasing corporate profits become an indication of good corporate performance. This result supports researches conducted by Nwangayu (2015) and Frank & James (2014). Cash flow negatively affect on performance due to their weak cash flow management

within the company so enable managers to pursue personal goals and the exclusion of shareholders' interests. In accordance with the Agency Theory that the agency conflicts arise because of differences of interest between shareholders to the manager. The main task of the manager is to manage the company resulting in a return / profit for shareholders and could increase net profit and cash flow. This results support the researches conducted by Nwakaego, et al (2015), Ali, et al (2013), Thanh & Nguyen (2013), Zhou, et al (2012). So the research hypothesis 1 & 2:

H1 : Operating cash flow has a significant positive effect on performance

H2 : Investing cash flow has a significant positive effect on performance

2) Debt and Performance

Debt is a resource borrowed with the expectation of paying back after a specified period of time. If the specified time spread over a period of one year then it becomes long term debt and if the expected payment period is less than or equal to one the it becomes a short term debt. (Kajirwa, 2015). Effect of debt on the performance can be positive or negative. Debt has a positive effect on performance due to debt funding will reduce the amount of conflict between shareholders and management. In addition, the debt would also reduce excess cash flow in the company thus reducing the possibility of waste made by management. This result support the researches conducted by Davydov (2016), Nirajini and Priya (2013), Nimalathasan & Valeriu (2010), Magaritis and Psillaki (2010). Meanwhile, if the debt negatively affects on performance because the debt risk for the company because it can affect the financial difficulties (financial distress). Debt levels also have an adverse impact on the company's performance because of high debt levels will tend to increase the interest expense, so companies have to cover such expenses through operating profit earned. A large interest expense will reduce the operating profit resulting in a decrease in net income, which means reduced profits. Iorpev & Kwanum (2012) proved that the short- and long-term debt has a significant negative effect on the performance in Nigeria. These results are supported by a study conducted by Vatavu (2015), Serghiescu and Vaidean, 2013), Soumadi & Hayajneh (2012), Anandasayanan & Subramaniam (2011), Onalapo and Kajola (2010). So hypothesis 3 and 4:

H3 : Short term debt has a significant negative effect on performance

H4 : Long term debt has a significant negative effect on performance

4. Research Methodology

4.1. Population and sampling techniques

The population is cement and ceramics industry in 2010 – 2014. Technique sampling is purposive sampling with certain criteria in accordance with the purpose of research. The criteria are as follows:

1. The companies were listed on the Indonesia Stock Exchange since January 2010 to December 2014.
2. Companies that publish annual reports during the observation period 2010-2014

Selected samples are 9 companies during 5 years so total 45 companies.

4.2. Definition of variables

1) Dependent variable is performance that measured by Return on Equity. The formula is:

$$\text{ROE} = \frac{\text{Net Income}}{\text{Shareholders equity}} \times 100\%$$

2) Independent Variables consist of four variables, they are:

a) Operating Cash Flow measured by operating cash flow divided by total cash flow. The formula is:

$$\text{Operating Cash Flow} = \frac{\text{OPCF}}{\text{Total Cash Flow}}$$

b) Investing Cash Flow measured by investing cash flow divided by total cash flow. The formula is:

$$\text{Investing Cash Flow} = \frac{\text{INFCF}}{\text{Total Cash Flow}}$$

c) Short term debt measured by current ratio. The formula is:

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

d) Long term debt measured by long-term debt divided by total assets. The formula is:

$$\text{Long-term Debt} = \frac{\text{Long-term debts}}{\text{Total assets}}$$

4.3. Empirical Model

Empirical model as follow:

$$\text{ROE} = \alpha + \beta_1\text{OPCF} + \beta_2\text{INFCF} + \beta_3\text{CR} + \beta_4\text{LTD} + \varepsilon$$

ROE is return on equity

OPCF is operating cash flow /total cash flow

INFC is investing cash flow/total cash flow

CR is current ratio

LTD is long term debt/total assets

5. The Findings

5.1 Descriptive Statistic

Tabel 4.1: Deskriptive Statistic

	ROE	OCF	INFCF	CR	LTD
Mean	8.057063	161.5418	5.813983	258.9993	16.72971
Median	21.81374	154.6692	-36.95488	170.5896	9.827673
Maximum	155.6079	3625.021	1740.137	698.2079	94.02413
Minimum	-625.4426	-2160.577	-1644.298	60.16919	0.339561
Std. Dev.	99.16108	1030.875	696.5004	185.7783	21.56440
Skewness	-5.913086	0.556383	0.408111	0.949472	2.131652

The average of return on equity is 0.08%, operating cash flow to total cash flow is 1.61%, investing cash flow to total cash flow is 0.05%, current ratio is 2.58% and long term debt to total assets is 16,72%. This industry has low return on equity that from 100% total equity can generate 0.08% net profit. But the companies have much operating cash flow and current ratio.

5.2. Panel Data Analysis

Testing panel data produces three outputs are *Pooled Least Square (PLS)*, *Fixed Effects Model (FEM)* and *Random Effects Model (REM)*. The output of the three will be selected which ones produce the best model.

5.2.1. Pooled Least Square (PLS) or Fixed Effect Model (FEM)

Selecting panel data model Pooled Least Square (PLS) or Fixed Effect Model (FEM), using Likelihood Ratio test (Chow Test). Then test the hypothesis:

H_0 : Jika Prob Cross Section Chi-square $\geq 5\%$, maka pilih *Pooled Least Square*

H_a : Jika Prob Cross Section Chi-square $< 5\%$, maka pilih *Fixed Effect Model*

Tabel 4.2: Likelihood Ratio (Chow Test)

Redundant Fixed Effects Tests
Pool: Untitled
Test cross-section fixed effects

Effects Test	Statistic	d.f.	Prob.
Cross-section F	0.703631	(8,32)	0.6860
Cross-section Chi-square	7.291820	8	0.5055

Source: *output Eview 9*

From the results in Table 4.2, Chi-square has p-value of 0.5055 (>5%), H0 failed rejected it means the accepted model is Pooled Least Square because it is better than Fixed Effect Model in this study. Then the next Hausman test is not necessary. Table 4.3 below estimation using Pooled Least Square Model:

Tabel 4.3: Pooled Least Square

Dependent Variable: ROE?
Method: Pooled Least Squares
Date: 05/24/16 Time: 05:34
Sample: 2010 2014
Included observations: 5
Cross-sections included: 9
Total pool (balanced) observations: 45

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	64.33667	31.94242	2.014145	0.0508
OCF?	0.002635	0.034817	0.075682	0.9400
INFCF?	0.000528	0.051830	0.010186	0.9919
CR?	-0.066466	0.080456	-0.826114	0.4136
LTD?	-2.360697	0.682628	-3.458251	0.0013***
R-squared	0.237167	Mean dependent var		8.057063
Adjusted R-squared	0.160884	S.D. dependent var		99.16108
S.E. of regression	90.83481	Akaike info criterion		11.96040
Sum squared resid	330038.5	Schwarz criterion		12.16114
Log likelihood	-264.1090	Hannan-Quinn criter.		12.03524
F-statistic	3.109030	Durbin-Watson stat		2.104888
Prob(F-statistic)	0.025571			

Source: *output Eviews 9*

From Table 4.3, operating and investing cash flow do not have significant effect on performance. High or low cash flow does not determine whether company's performance is good or bad. And current ratio does not have significant effect on performance. The company is not dependent on short-term funding to produce a high net income. Long term debt has a significant negative effect on the performance at the level of 1% . It shows that these types of companies have to reduce long-term debt to produce high performance. This result supports the researches conducted by Vatavu (2015), Serghiescu and Vaidean, (2013), Soumadi & Hayajneh (2012), Anandasayanan & Subramaniam (2011), Onalapo and Kajola (2010).

6. Conclusions and Recommendations

This result shows that long term debt has a significant negative effect on performance. It proves that this industry is more likely to reduce the use of a debt to improve its performance. Funding chosen is internal fund namely retained earnings. This result supports pecking order hypothesis. Based on this result, companies should be increased net profit by optimizing operational activities and minimizing costs. The addition of a debt should be able to be used to increase the capacity of production and sales. Indonesia is currently in development stage, so companies of cement and ceramics industry have good prospect in the future. For investors who would invest in this industry choose a company that has a relatively low debt and high retained earnings. For further study researchers can explore other variables such as size, managerial ownership, tangibility, taxes and growth.

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