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The Macroeconomic Impact On Investment Decisions in manufacturing companies Listed on the Indonesia Stock Exchange (BEI)

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Abstract

The aim of this research is twofold: 1) to examine and analyze how interest rates, inflation, and exchange rates impact investment decisions, and 2) to explore how interest rates, inflation, exchange rates, and investment decisions affect the value of manufacturing companies listed on the Indonesia Stock Exchange.This study adopted a causal approach using secondary data gathered from financial statements of manufacturing companies listed on the Indonesia Stock Exchange, obtained from various sources including the Indonesian Capital Market Directory (ICMD) data via the Capital Market Information Center (PIPM) Makassar office, the Indonesia Stock Exchange website, the Bank of Indonesia website, and the Badan Pusat Statistic (BPS) website. The population of this study consisted of all manufacturing companies listed on the Indonesian stock market. The sampling technique used was purposive sampling, which resulted in 45 companies being selected, each with financial statements covering a 5-year period, thereby providing a total of 225 observations. The method of analysis used in this study was path analysis. The findings revealed that interest rates and inflation have a negative impact on investment decisions, while exchange rates have a positive impact.

Keywords: Interest Rate, Inflation, Exchange Rate and Investment Decision

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INTRODUCTION

Indonesia's capital market, particularly the Indonesia Stock Exchange (BEI), is considered an emerging market that is vulnerable to macroeconomic conditions. The 1998 economic crisis was a turning point in the country's economic development as it marked the collapse of its economic pillars. The crisis began with a decrease in public confidence in Indonesian banks, leading to massive withdrawals of funds by depositors (run), which were then taken abroad (capital flight). The crisis was further compounded by a 70% increase in interest rates and a 500% depreciation of the rupiah against the US dollar, resulting in a disruption of almost all economic activities. The capital market was hit hard and experienced a decline in public confidence. Stocks began to plummet, causing investors to suffer significant losses. This was surprising, as stocks were sold at a mere Rp 10 per share and the Composite Stock Price Index (CSPI) had never dropped below 300.

Similarly, in 2008, the global recession was triggered by the crisis in the United States. The crisis caused a deep recession in the US economy, the effects of which are still being felt today. Major banks such as Lehman Brothers were affected by this crisis, as well as the US stock market on Wall Street. The Indonesian capital market also felt the impact of the crisis, with a two-day closure in December 2008.

Osoro (2014) noted that macroeconomic variables significantly influence business activity. The macroeconomic environment has a substantial effect on the business environment, as confirmed by the studies of Ravindran (2015), Ratnawati (2007), and Akingunola (2012), which reveal that external factors have a positive and significant effect on investment decisions. Taofik (2010) also found that the macroeconomic environment, particularly inflation, has a significant impact. Caroline (2012) similarly argued that inflation has a significant influence on the performance of the stock market.

Chen et al. (2006) found that macroeconomic variables have a systematic impact on stock market returns. The strength of the economy affects the discount rate, a company's ability to generate cash flow, and future dividend payouts, indicating the significance of macroeconomic variables in the stock market (Maysami and Sim Koh, 2000). In particular, interest rates have had a significant negative impact on the Jakarta Composite Index (JCI) since 2003. Continuation of this trend is expected to further undermine the performance of the Indonesia Stock Exchange. The sensitivity of approximately 0.5 implies that a 1% increase in interest rates would result in a 0.5% decrease in the composite stock price index, and conversely, a 1% decrease in interest rates would result in a 0.5% increase in the JCI.

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Inflation is a major contributor to the rise in interest rates, as higher interest rates mean higher interest costs. Companies with high debt will be especially impacted by rising interest rates. In addition, the cost of raw materials will increase, and if companies cannot pass on these costs to consumers, their profitability will decrease. This decrease in profitability will negatively impact the dividend income that investors expect to receive, causing investing in stocks on the capital market to become less appealing. Consequently, investors may shift their investments to other opportunities that can offer higher returns, such as bank deposits, during periods of high interest rates.

Nartea et al. (2014) have highlighted the significance of exchange rates and inflation in affecting stock prices. The control of money supply and inflation plays a critical role in managing exchange rates and inflation, where interest rates act as a medium to regulate their effects on share prices. The fluctuations in stock prices triggered by changes in exchange rates and inflation can impact the returns and a reasonable rate of return. Additionally, the movement of exchange rates and inflation can create an investment-friendly climate that can attract both domestic and foreign investors to invest their capital in the country, leading to benefits for both the investors and the country.

It is important to note that macroeconomic factors have a significant impact on the performance of the manufacturing industry, as shown in Table 1. This includes indicators such as Return on Equity (ROE) and Price Earning Ratio (PER) during the period of 2010-2014 in the IDX.

Table 1. Indonesia Macro Economy Factor Indicators, Average Growth Return on Equity (ROE), and Price Earning Ratio (PER) Manufacturing Industry in IDX Period 2018-2022

Year	Inflation Rate (%)	Interest Rate of SBI (%)	Exchange Rate USD Against USD (Rp)	*Return on Equity* (ROE) (Rp)	*Price Earning Ratio* (PER) (%)
2018	5,13	6,50	9.583	24,57	16,67
2019	5,38	6,60	9.279	25,62	32,96
2020	4,28	5,75	9.881	27,28	15,09
2021	6,97	7,02	10.951	25,82	13,36
2022	6,42	7,54	12.373	24,13	13,80

Source: Bank of Indonesia and Indonesia Stock Exchange (2022)

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The following problem formulation can be proposed based on the background description: 1) Interest rate affects investment choice of quoted manufacturing firms, 2) Inflation affects investment choice of quoted manufacturing firms, 3) Currency rate affects investment choice of quoted manufacturing firms.

LITERATURE REVIEW

Interest rate

Interest rates refer to the amount of money that is paid for the use of borrowed funds, as explained by Wardane (2003) in Prawoto and Avonti (2004). The interest rate is the cost of borrowing money, and it is measured as the amount of interest that has to be paid for each unit of time. The supply and demand of money determine the interest rate, according to Keynes in Wardane's (2003) view. Changes in interest rates can impact investment decisions, especially in securities, where prices may rise or fall depending on the interest rate. When interest rates increase, securities prices may fall, and vice versa. As a result, the holder of securities may suffer a capital loss or gain. There are two types of interest rates: nominal interest rates, which are the rate of interest in terms of monetary value, and real interest rates, which are the interest rates adjusted for inflation by subtracting the inflation rate from the nominal interest rate.

The Accounting Dictionary (1996: 69) defines interest as the cost of using money over a period and as a share of ownership or a portion of equity in a company, trading business, or power source. The factors that influence interest rates include the terms of the loan, the level of risk involved, liquidity of the assets, and administrative costs. Loans with longer terms generally offer higher interest rates than short-term ones. Some loans are considered riskless, while others are highly speculative. Liquidity is the ease with which assets can be exchanged for cash with minimal loss in value. Administrative costs associated with loans can vary widely, with high administrative costs leading to higher interest rates. According to Tandelilin (2001), high interest rates can negatively affect the present value of a company's cash flow, leading to decreased investment opportunities and a subsequent drop in stock prices and the company's overall value.

Inflation.

Inflation is an ongoing process of increasing prices of goods, where the increase in prices of individual items may not be uniform in either absolute or percentage terms and may occur at different times. The overall rise in prices happens over a period of time

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and not just a one-time increment. To measure inflation, various price indexes such as the Consumer Price Index, Wholesale Price Index, and GNP Deflator are used. It is important to note that inflation is not just an economic phenomenon but is also influenced by political decisions and sociological background of society. For example, the inflation that occurred in Indonesia during the turbulent period around 1965 and inflation in Latin American countries today cannot be viewed simply as an economic disease that can be solved by economic therapy Kasmi et al. (2022).

Noise inflation is a temporary component of the inflation rate that occurs due to occasional shocks on the rate of inflation. The factors that may cause temporary upheaval include increased production and distribution costs, increases in energy and transport costs, and non-economic factors such as social unrest, floods, earthquakes, and forest fires. These factors can lead to prolonged inflationary pressures if the economy has inefficient and unbalanced fundamental micro structures, especially in the production and distribution sectors Mastuti et al. (2022).

Exchange rate refers to the price of a country's currency against the currency of other countries. It is the value of one currency translated into another country's currency, for example, the exchange rate of the rupiah against the US Dollar or the exchange rate of rupiah against the yen. The exchange rate is one of the indicators that affect activity in the stock market and money market as investors tend to be cautious when making investments. Therefore, the negative influence of the Rupiah exchange rate against foreign currencies, especially the US Dollar, can impact the economy and capital market negatively (Sitinjak and Kurniasari, 2003, cited in Adiningsih et al., 2008, p. 155).

Exchange Rate

Exchange rates are influenced by various factors, including fundamental, technical, and market sentiment factors. According to Madura (2003), the factors are as follows:

1. Fundamental factors, These factors are related to economic indicators such as inflation, interest rates, the relative differences in inter-country revenues, market expectations, and central bank interventions. The actions of central banks, for instance, can influence the value of a country's currency.

2. Technical factors, These factors relate to the supply and demand of foreign exchange at certain times. If there is an excess demand, while the offer is fixed,

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the forex price will go up and vice versa. Technical factors also include the volume and speed of transactions and the level of liquidity in the market.

3. Market sentiment, Market sentiment is driven by incidental rumors or political news, which can lead to sharp increases or decreases in forex prices in the short term. However, once the rumors or news have passed, the exchange rate is likely to return to normal.

Several factors affect the movement of exchange rates, according to various literature sources such as Jeff Madura (1993). These factors include fundamental factors, technical factors, and market sentiment. Fundamental factors refer to economic indicators like inflation, interest rates, inter-country revenue disparities, market expectations, and central bank interventions. Technical factors relate to the supply and demand conditions of foreign exchange at specific times, with excess demand causing an increase in forex price and vice versa. Meanwhile, market sentiment is influenced by incidental rumors or political news, which may either increase or decrease forex prices, with prices eventually returning to normal after rumors or news have passed.

Several research studies, such as those conducted by Olweny and Omondi (2011), Richard (2012), Divianto (2013), Cliff and Willy (2014), and Ramasamy and Abar (2015), have found a correlation between share prices and exchange rates. Therefore, it can be concluded that exchange rates have a causality relationship with stock returns, which reflect a company's performance in carrying out its operations. Net income is one of the benchmarks for measuring a company's success, so a strong correlation should exist between exchange rate changes and changes in net income.

Investation decision

Investment is a term with a broad definition. It can be interpreted as the sacrifice of current consumption for future consumption or how much consumption an individual or group is willing to give up now for the same level of satisfaction in the future. When related to the capital market, investment is defined as investing in financial assets to obtain profits, which is not independent of possible risks.

Economists have proposed various notions of investment. Francis (1991:1) suggests that investment is a commitment of money that is expected to generate additional money in the future. According to Francis, investment is like planting money to reap additional money later on. Hirt (1993:15) defines investment as the commitment of current funds in anticipation of receiving a large flow of funds in the future. Hirt sees

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investment as taking responsibility for current funds in the expectation of receiving a significant flow of funds in the future.

Investment decisions involve the future, which contains uncertainty and risks for investors. Therefore, having knowledge of risk is crucial for potential investors and investors..

A rational investor must consider two important factors before making an investment decision: the expected return and the level of risk involved. Investment involves the commitment of a certain amount of current funds with the expectation of generating returns in the future. However, compared to other investment alternatives such as bonds, deposits, and savings, investing in stocks entails a higher level of risk. The risk associated with stock investment is reflected in the variability of returns on both individual and market levels, and can be measured by the variance or standard deviation of the return, according to Francis (1991: 18).

Investment entails uncertainty, where the profit that will occur cannot be known for certain, but can be arranged in a possible alternative event that can be known. As stated by Sumantoro (1990: 14), investment is an activity that involves investing capital either directly or indirectly with the hope of generating profit from the investment in the future. Jogiyanto (2000: 5) defines investment as the postponement of current consumption to facilitate efficient production over a certain period of time. Similarly, Ahmad (2006: 3) defines investment as the placement of money or funds in the hope of gaining additional or profitable returns.

Investment decisions are influenced by various factors, including investment objectives, risk tolerance, time horizon, and market conditions. A rational investor should have clear investment objectives and a well-diversified portfolio to manage risks. The investment decision-making process involves analyzing various factors such as the company's financial statements, market trends, economic indicators, and industry outlook.

In terms of investment opportunities, companies with high growth potential are often considered attractive investment options as they offer the possibility of generating high returns. However, investing in growth companies can also be risky as there is no guarantee that the expected growth will materialize. Therefore, investors should carefully assess the growth potential of a company and its ability to generate returns in the future. The investment opportunity set (IOS) provides a framework for evaluating a company's growth opportunities and the potential returns they can generate.

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In summary, investment decisions involve analyzing various factors such as risk, return, growth potential, and market conditions. A rational investor should have clear investment objectives, a well-diversified portfolio, and a thorough understanding of the investment opportunities available to them.

Additionally, the investment decision-making process is influenced by various factors, including macroeconomic factors such as economic growth, inflation, interest rates, and government policies. Microeconomic factors such as industry conditions, competition, and firm-specific factors such as financial condition, management quality, and corporate strategy are also important considerations.

Moreover, behavioral factors such as cognitive biases, emotions, and social influences can also affect investment decision making. These factors may lead investors to make irrational decisions and deviate from traditional economic assumptions of rationality. Understanding these behavioral factors is important in developing effective investment strategies and minimizing potential losses.

Overall, investment decisions are crucial for both individual and corporate financial success. Making informed and rational investment decisions requires a thorough understanding of the investment landscape, including risks and potential returns, as well as a consideration of various factors that may influence the decision-making process.

Conceptual Framework

The financial management function involves various activities such as investment decisions, financing decisions, and dividend decisions. Investment decisions involve choosing the appropriate investment opportunities that generate the highest return with the lowest risk. Financing decisions involve identifying the optimal capital structure of the company and raising funds from different sources such as debt and equity. Dividend decisions involve determining the proportion of profits to be distributed to shareholders and retaining profits for future investments.

Investment decisions are crucial for achieving the company's objectives because they determine the future growth and profitability of the company. The investment opportunity set (IOS) is an essential concept in investment decisions as it represents the combination of assets in place and future investment options that have positive net present value. IOS is critical in estimating the company's prospects and future expenditure sets that are expected to result in greater returns.

Financing decisions are also critical for achieving the company's objectives as they determine the optimal capital structure and the ability to raise funds for investments. The

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capital structure represents the mix of debt and equity financing used by the company. The optimal capital structure is achieved by balancing the benefits of debt (tax shield and lower cost of capital) against the costs of debt (financial distress costs).

Research Conceptual Framework

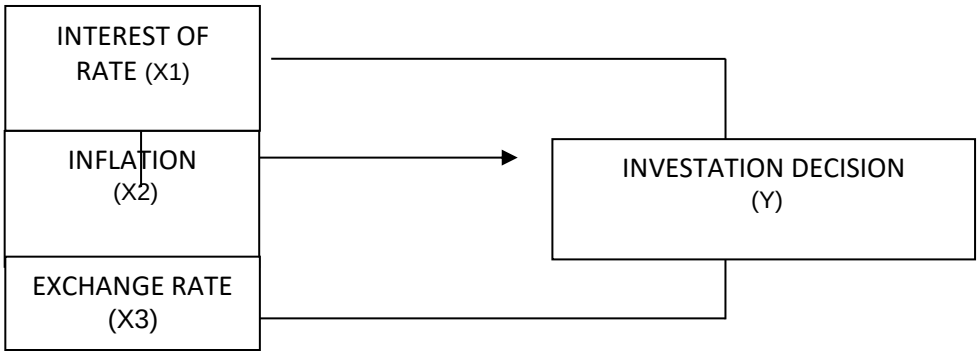


Figure 1. Conceptual Research Framework

METHODOLOGY

Research Design

This study uses a quantitative research design with panel data analysis. Panel data analysis is used to analyze data from a panel or a group of individuals, in this case, the selected manufacturing companies listed on the Indonesia Stock Exchange. This research design is chosen because it allows for the analysis of both time-series data and cross-sectional data, which is suitable for analyzing the relationship between investment opportunity set and firm value over time.

Data Collection

The data used in this study are secondary data obtained from financial reports of the selected companies listed on the Indonesia Stock Exchange, as well as from other relevant sources such as the Central Bureau of Statistics (BPS) and Bank Indonesia. The data collected includes the variables of investment opportunity set, firm value, profitability, liquidity, leverage, and firm size. The data will be collected for a period of five years, from 2018 to 2022.

Research sites This research is conducted at Indonesia Stock Exchange (IDX) by accessing data through Makassar Capital Market Information Center (PIPM), as well as

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through IDX, Bank Indonesia and Central Bureau of Statistics (BPS) website. Population and Sample. The population of this study are all Go Public Manufacturing companies listed on the Indonesia Stock Exchange (BEI), with observation period of 2018 to 2022. In accordance with ICMD number of manufacturing companies listed on the BEI 2018 - 2022 as many as 113 companies. The technique used in sampling is by using Purposive Sampling. The sample used in this research is 40 companies.

Analysis of Data

The multiple regression analysis equation used in this research is:

Investment Decision ($(Y) = \alpha_1 + \beta_{11} X_1 + \beta_{12} X_2 + \beta_{13} X_3 + \varepsilon$

where:

Investment Decision is the endogenous variable

Interest Rate, Inflation, and Exchange Rate are the exogenous variables

β0 is the intercept coefficient

β1, β2, and β3 are the regression coefficients for Interest Rate, Inflation, and Exchange Rate, respectively

ε is the error term

The purpose of this analysis is to examine the relationship between the independent variables (Interest Rate, Inflation, and Exchange Rate) and the dependent variable (Investment Decision) and to determine the strength and significance of these relationships. The results of the analysis will be used to draw conclusions about the impact of these variables on investment decisions in the manufacturing companies listed on the Indonesia Stock Exchange.

RESULT & DISCUSSION

Analysis of Interest Rate, Inflation and Exchange Rate on Investment Decision

1. Simultaneous Testing

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ANOVA[b]

Model		Sum of Squares	df	Mean Square	F	Sig.
	Regression	318.916	3	106.305	.326	.806[a]
	Residual	72026.701	221	325.913		
	Total	72345.617	224			

a. Predictors: (Constant), X3, X2, X1
b. Dependent Variable: Y

Model Summary[b]

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Durbin-Watson
1	.066[a]	.004	-.009	18.05305	1.983

a. Predictors: (Constant), X3, X2, X1
b. Dependent Variable: Y

Based on the results of the simultaneous testing using ANOVA table, it can be seen that the value of F is 0.326 with a probability (sig) of 0.806. Since the value of sig > 0.05, the null hypothesis (H0) is accepted and the alternative hypothesis (Ha) is rejected. This means that interest rates, inflation, and exchange rates together have no significant effect on investment decisions.

The coefficient of determination or R square is 0.004 or 0.4%, which means that the exogenous variables (interest rates, inflation, and exchange rates) explain only a small portion of the variation in the endogenous variable (investment decision). The remaining 99.6% of the variation in investment decision is explained by other variables not included in the model.

Therefore, based on the results of the simultaneous testing, it can be concluded that interest rates, inflation, and exchange rates do not have a significant impact on investment decisions of the manufacturing companies listed on the Indonesia Stock Exchange from 2018 to 2022. However, it is important to note that there may be other

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variables not included in the model that may have a significant impact on investment decisions.

2. Partial Testing

Coefficients[a]

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	8.660	17.145		.505	.614
X1	-.564	5.024	-.019	-.112	.911
X2	-.896	2.692	-.048	-.333	.740
X3	.002	.002	.096	.904	.367

a. Dependent Variable: Y

Based on the partial testing results, it can be concluded that none of the independent variables (interest rate, inflation, and exchange rate) have a significant effect on investment decision. The sig values for all variables are above 0.05, indicating that the null hypothesis (H0) is accepted and the alternative hypothesis (Ha) is rejected. Therefore, it can be inferred that in this particular study, changes in interest rate, inflation, and exchange rate do not affect the investment decision. However, it is important to note that this result may vary depending on the context of the study and the sample used.

DISCUSSION OF RESEARCH RESULTS

The research findings demonstrate that the Interest Rate (X1) variable has a negative and significant effect on the investment decision (Y), with a value of -0.564 and a probability level of 0.911. This indicates that interest rates have a negative impact on investment decisions due to the tendency of investors to deposit their funds in banks when interest rates increase, as bank savings are considered less risky than real and financial investments. These results align with previous research, which found a negative correlation between interest rates and JCI performance, showing that higher interest rates

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lead to weaker stock exchange performance. Specifically, a 1% increase in interest rates leads to a 0.5% decrease in the composite share price index, while a 1% decrease in interest rates leads to a 0.5% increase in JCI. The study supports the notion that macroeconomic variables significantly influence business environment and activity, as shown by the findings of Osoro (2014). However, it contradicts the previous research by Ravindran (2015), Ratnawati (2007), and Akingunola (2012), which suggested that external factors have a positive impact on investment decisions. According to Bialowolski (2012), external factors such as law, economic growth, taxes, interest rates, and stock market conditions can impact the value of companies..

The results of the research indicate that the variable of inflation (X2) has a negative and significant effect on investment decisions (Y), with a coefficient of -0.896 and a probability level (Sig) of 0.740. This means that inflation has a negative impact on corporate investment decisions. High inflation leads to increased production costs, which ultimately results in lower profit margins for companies and a decline in stock prices in the market. Moreover, it reduces the value of profits and the purchasing power of investment capital, which further affects the JCI. These effects are not immediate but occur over time. The findings of this study contradict the research conducted by Taofik (2010) and Caroline (2012) that suggest inflation has a significant influence on stock performance. However, they are consistent with the research conducted by Osoro (2014) that macroeconomic variables greatly influence business environment, and they are also in contrast with the research conducted by Ravindran (2015), Ratnawati (2007), and Akingunola (2012) that claim external factors have a significant and positive impact on investment decisions.

Based on the research results, the Exchange Rate variable (X3) has a positive coefficient of 0.002 with a probability level (Sig) of 0.360, indicating a very small and insignificant effect on investment decisions (Y) in the company. However, it is important to note that exchange rate movements can impact international competitiveness, trade balance positions, and the real output of a country, which may have future implications for a company's cash flow and stock prices. Previous research has shown mixed results regarding the relationship between capital market and exchange market. Aggarwal (1999) found a positive association between stock market returns and US dollar revaluation, while Soenen and Hennigar (2000) found a negative relationship. Roll (2002) found a positive relationship between the two markets, and Chow et al (2007) found no significant relationship between stock returns and exchange rate returns using monthly data for the period 2000-2005.

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CONCLUSION

In conclusion, this research has revealed important insights regarding the relationship between macroeconomic variables and investment decisions in the manufacturing sector. Firstly, the study found that interest rates have a negative and significant impact on investment decisions, indicating that higher interest rates will decrease investment in the manufacturing sector. Secondly, the study showed that inflation rates also have a negative and significant effect on investment decisions, suggesting that an increase in inflation will lead to a decrease in investment decisions for manufacturing companies. Thirdly, the study found that exchange rates have a positive effect on investment decisions, indicating that exchange rate movements can influence investment decisions in the manufacturing sector. These findings provide important implications for policymakers and investors in understanding the factors that affect investment decisions in the manufacturing sector.

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