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Measuring the Company's Financial Performance from Working Capital, Liquidity, and Solvency

Yunus Harjito[1*], Sapna Eka Anggrahini[2], Faiz Rahman Siddiq[3]
yunus.harjito@gmail.com[1], sapnanana54@gmail.com[2], faiz.usb@gmail.com[3]*
[1,2,3] Universitas Setia Budi, Surakarta

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Abstract
This study aims to analyze the effect of Working Capital Efficiency, Liquidity and Solvency on the Company's Financial Performance. To find out the extent to which a company has implemented using the rules of financial implementation properly and correctly, it can use financial performance instruments. The population of this study is a cosmetic company listed on the Indonesian Stock Exchange for the period 2015-2022. The sample of this study amounted to 48 samples obtained from 6 companies for 8 years with purposive sampling method. The analysis technique used focuses on multiple regression analysis using the SPSS application. The results showed that Working Capital Efficiency proved to have a significant negative effect on the Company's Financial Performance, while Liquidity and Solvency were not proven to have an influence on Financial Performance.

Introduction

The profit of a company reflects the financial situation evaluated using financial analysis instruments to assess good or bad financial conditions, which reflect the company's performance in a certain period. This is important to ensure optimal use of resources in the face of environmental changes (Oktarina, 2020). Furthermore, the company will be considered healthy if the ability in its financial performance from year to year is getting better. During the Covid-19 pandemic, it was common for companies to experience a slump in financial performance. There are several top industries that have experienced the greatest impact due to the Covid-19 pandemic, including Film is a company that is vulnerable to Covid-19. Of course, there are many film productions, especially the circulation of films has stagnated because all theaters are closed.

Although various industries have experienced a decline, the cosmetics industry has actually experienced growth due to the large market potential. This is because beauty and body care products are now not only considered a desire but a necessity, especially for women. As the demand for these products increases, cosmetic companies compete to create new products and brands to maximize their profits. Even in 2020, the beauty industry in Indonesia is predicted to experience the most growth compared to other countries in Southeast Asia (Pramita, 2017). According to data published by Statista's Research Department on June 1, 2023, market revenue for the beauty and personal care industry in Indonesia from 2018 to 2027 continues to increase year-on-year.

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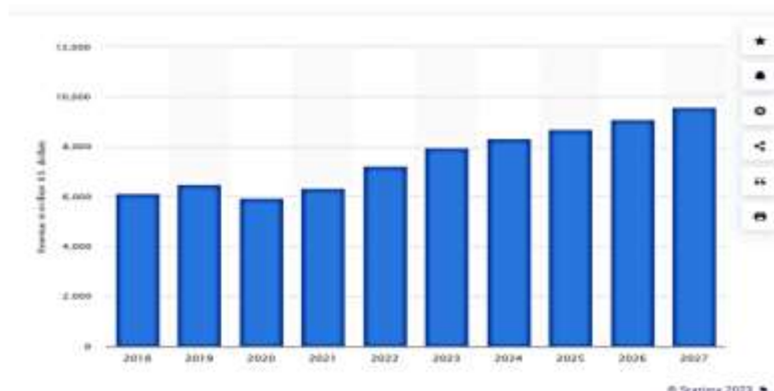

Figure 1. Beauty Industry Revenue Growth

Global trends have spread and influenced the way people go about their daily beauty and grooming routines, impacting revenue growth in the cosmetics industry (Statista, 2022). According to information from the Central Bureau of Statistics (BPS), the cosmetics industry sector, which includes pharmaceuticals, chemicals, and traditional medicines, experienced a growth of 9.61% in 2021. In addition, BPOM RI noted that the increase in the number of companies in the cosmetics industry reached 20.6%. This data illustrates the great potential and opportunities in the cosmetics industry, especially in Indonesia (CNBC Indonesia). Sutomo (2014) explains that every company has the same goal, which is to achieve maximum profit to reflect a good level of profitability. Profit is often used as a measure of a company's financial performance, which is the basis for making investment decisions and for forecasting expected changes in future profits. This affects the decisions of investors and potential investors who plan to inject their capital into the Company.

One way that the company's financial performance can improve is by carrying out effective working capital management as the key to the company's success. Working capital must be available and continuously rotating within the company. If the company is unable to manage working capital properly, it can lead to slow working capital turnover, which in turn extends the period of return or receipt of cash. This means that the need for working capital is increasing Purwanti et al. (2022). Moreover, working capital efficiency will have an impact on profitability, which is a measure of the company's financial performance (Wijaya & Isnani, 2019; Nugraha et al., 2020; Purwanti et al., 2022; Sari et al., 2023; Anissa, 2019; Mahulae, 2020; Irianti, 2021). In addition, financial performance as measured using profitability is also influenced by liquidity (Mahardika and Suci, 2021), but these results contradict the results of research conducted by Purwanti et al. (2022), and Gultom et al (2020), and Wage et al (2021).

The solvency ratio reflects the ability of a company to meet its long-term obligations or debts in a liquidation situation. This ratio can be calculated by considering elements such as fixed assets and long-term debt (Susilawati, 2012). The solvency ratio also indicates how much the company's operational activities are supported by debt, which is proportional to the use of the company's own capital (Supatmin, 2021). Sari et al (2023) explain that solvency has a positive effect on profitability which is a measure of financial performance. In line with this, the proven influence between solvency and profitability as a measure of financial performance is supported by the results of Sari's research (2023); Rahmah et al (2019); Nugraha et al (2020); and Bintara (2020).

The results of previous research which still show inconsistencies in research on the company's financial performance are the basis for the need to conduct this research. In addition, this research is also important to be carried out not only for the subjective justification of the researcher but also based on the phenomena that occur and previous research.

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Brigham and Hauston (2014) explain that a signal is a step taken by a company to provide information to investors about management's view of the company's prospects. This signal is in the form of information about the strategies implemented by management to meet the expectations of company owners. The information conveyed by the company has important significance because it affects investment decisions from parties outside the company. This information is crucial for investors and businesspeople because it creates information asymmetry between the company and external parties such as investors and creditors, where the company has deeper access to information about the company's condition and future projections.

Indicators of the company's financial performance can be seen from the level of profitability obtained by the company while running its business. Profitability is the ability of a company to create profits from its operational policies and decisions over a certain period. A high level of profitability is often a key indicator of company performance, illustrating how well the company operates and manages its business activities.

Working capital efficiency occurs when the working capital turnover period is shorter, indicating a more efficient use of working capital by the company. This can increase the level of profitability, as explained by Wijaya and Isnani (2019). When working capital turnover is fast, revenue from sales can effectively cover operating costs. Conversely, if sales decline, the company may face difficulties in meeting operational needs, which may affect the profitability or financial performance of the company (Wijaya and Isnani, 2019). Working capital needs to be sufficiently available and well managed because a lack of working capital will result in reduced profits (Musthafa, 2017). The more efficient working capital can increase the profitability (a measure of financial performance) of the company (Sari et al, 2023; Ermanda and Purnamawati, 2017; Wibowo and Wartini, 2012; Anissa, 2019; Mahulae, 2020; and Irianti, 2021). From the results of the description above, the following hypothesis can be formulated:

H_1: Working capital efficiency has a positive effect on the Company's Financial Performance.

Company liquidity is a measure used to assess the company's ability to meet financial obligations that must be completed soon. Liquidity reflects the extent to which the company can overcome financial obligations that must be met immediately, as explained by Mufidah, et al. (2018). The higher the liquidity, the stronger the company fulfills the obligations that must be paid immediately, however, if it is too high, it will affect the company's profitability (Zulkarnain, 2020). Liquidity can be used as a measure to reflect management performance in managing working capital whose funding comes from current debt and company cash (Daud, 2017). Too high liquidity indicates too many current assets owned by the company, which will affect profitability to be unfavorable (Yuniningsih, 2018). The results of previous research show that liquidity affects profitability which is an indicator to measure financial performance (Sari et al., 2023; Manik and Sari, 2023; Novita and Sofie; 2015; Rahmah, et al., 2019; Marinda, 2021; and Nurdiana, 2018). Based on the explanation above, the following hypothesis can be formulated:

H_2: Liquidity has a positive effect on the Company's Financial Performance.

Dewi (2017) explains that the solvency ratio is a ratio used to measure the amount of debt used to finance the company's assets. The solvency ratio measures how effectively the company is financed with debt (Purwanti et al., 2022). Solvency reflects the company's ability to meet its financial obligations in the event of liquidation (Wijaya and Isnani, 2019). Companies with high solvency levels tend to face greater risks, namely the potential for decreased profitability because more of the revenue earned is used to pay debt interest expenses. This condition also indicates that the company may rely on external capital more than its own capital in its operational activities. Sari et al. (2023) revealed that solvency affects profitability (one of the company's financial performance indicators. This is also reinforced by the results of research conducted by Sari (2023), Rahmah et al. (2019), Nugraha et al. (2020), and Bintara (2020). So that from this description, the next hypothesis can be formulated, namely:

H_3: Solvency has a negative effect on the Company's Financial Performance.

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The relationship between the independent variable and the dependent variable in this study can be explained by the following model:

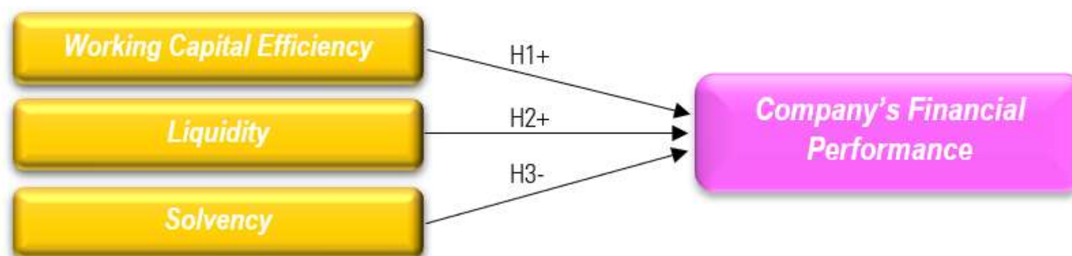

Figure 2
Research Framework

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Methodology

This study uses an associative method research design and type with a quantitative approach. Sugiyono (2019) explains that the associative method aims to identify the relationship between two or more variables. On the other hand, a quantitative approach is a research method based on the philosophy of positivism and applied to analyze data from a particular population or sample. The population in this study were all cosmetic companies listed on the Indonesia Stock Exchange. In this study, the sample was determined using a purposive sampling approach. The criteria used to determine the sample are: Cosmetic companies that are listed and still active on the Indonesia Stock Exchange for the period 2015-2022, cosmetic companies that publish financial reports and have complete and audited financial data. The data analysis method used is multiple regression analysis using the IBM SPSS 25 application. The operational definitions and variable measurements in this study can be presented as follows:

Table 1. Operational Definition and Variable Measurement

Variable	Variable Definition	Indicator
Company's Financial Performance	Financial performance is measured using profitability, which is a ratio used to measure the company's ability to earn profits, in relation to sales, assets and profits and own capital (Sujarweni, 2019).	$Return\ On\ Asset = \frac{Net\ Income}{Total\ Assets}$
Working Capital Efficiency (WCE)	The shorter the working capital turnover period, which means that the faster the working capital rotates, which results in higher working capital turnover, meaning that the company is more efficient which will have an impact on higher profitability (Kasmir, 2019).	$WCE = \frac{Net\ Sales}{Current\ Assets - Current\ Liabilities}$
Liquidity	Is the company's ability to meet short-term obligations or debts that are due when billed simultaneously. This ratio is measured using Current Ratio (CR).	$CR = \frac{Current\ Assets}{Current\ Liabilities}$
Solvency	is a ratio used to measure the extent to which the company's assets are financed with debt (Kasmir, 2019). This ratio is measured using the Debt to Asset Ratio (DAR).	$DAR = \frac{Total\ Liabilities}{Total\ Assets}$

Result And Discussion

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Results

The classic assumption test results show that the data is normally distributed with testing using the One-Sample Kolmogorov-Smirnov Test resulting in a significance value of 0,068 (>0,05). In addition, the results of data analysis also show that the data is free from multicollinearity, heteroscedasticity, and autocorrelation.

The results of hypothesis testing using multiple regression analysis can be presented as follows:

Table 3. Multiple Linear Regression Analysis Results

No.	Hypothesis	B	Sig.	Result
1	H_1: Working capital efficiency has a positive effect on the Company's Financial Performance.	-0,012	0,018	Significant
2	H_2: Liquidity has a positive effect on the Company's Financial Performance	0,008	0,525	Not Significant
3	H_3: Solvency has a negative effect on the Company's Financial Performance	0,249	0,170	Not Significant

Source: Data Processed, 2024

The next test results are to determine the Adjusted R Square value and Anova test with the following results:

Table 4. Adjusted R Square Value and Anova Test

No.	Description	Score	Sig.
1	Adjusted R Square	0.262	
2	Anova	F= 6,202	0,001

Source: Data Processed, 2024

Discussions

The test results show that the Working Capital Efficiency variable has a significance level of 0.018 with a beta value of -0.012. So that working capital efficiency has a significant negative effect on the company's financial performance. The results of this study support the research of Nugraha et al. (2020) which states that working capital efficiency has a negative effect on financial performance. In line with this, this research is also supported by research conducted by Purwanti et al. (2022) which states that there is a negative influence between working capital efficiency on financial performance. During the 2015-2022 period, the cosmetics industry experienced many changes including an increase in demand for natural and organic products, as well as a shift towards online sales. Companies adjusting their working capital strategies to invest in these trends can increase profitability despite a decrease in short-term working capital efficiency. Therefore, it is important for companies to achieve the right balance in working capital management.

The significance value of the liquidity variable is 0.525 (>0.05), this indicates that liquidity has no effect on financial performance proxied by profitability. This shows that the proportion of high or low liquidity does not always affect the level of profitability directly. Data analysis shows that although the liquidity of cosmetics companies fluctuates from year to year, their average profitability has increased. This indicates that high liquidity is not always directly proportional to high profitability, because funds that are not managed properly can hinder the company's operations. The cosmetics industry often has large profit margins, with products sold at significant markups. As a result, while liquidity may not be optimal, high profit margins can still maintain a company's profitability. In addition, external factors such as economic conditions, competition, and regulatory changes also play a role in affecting profitability. These results are in line with research conducted by Pinasthika (2022) and Gultom et al. (2020).

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The test results show that the significance value is 0.170 (>0.05) so that it can be explained that solvency has no effect on financial performance proxied using profitability. This means that high or low solvency does not guarantee that the company will experience increased profitability. Because corporate debt cannot provide opportunities for profit, the use of debt is not for funding the company's operational activities which can have an impact on profitability. Cosmetic companies utilize debt to fund investment in products, including research and development of new products, marketing, and market expansion. In accounting, this is reflected in increased assets and revenues that can cover long-term liabilities. Companies that have strong and stable operating income are less affected by high debt levels. If operating income is large enough to cover interest and principal costs, a high debt ratio will not significantly reduce profitability. This result is supported by research conducted by Wibowo and Wartini (2012) and Purwanti et al. (2022).

Conclusions

This study examines the effect of Working Capital Efficiency, Liquidity and Solvency on Financial Performance proxied by profitability. Based on the data analysis that has been done, the results show that Working Capital Efficiency affects Financial Performance, but Liquidity and Solvency have no effect on Financial Performance.

Limitations

This study proxy's liquidity with Current Ratio, but the results of this study have no effect, as well as solvency which is proxied by Dapt to Asset Ratio which shows no effect. So that further research for liquidity variables is recommended to use other proxies such as quick ratio or cash ratio to get better results. The results of the Adjusted R Square show 0.262 or 26.2% which indicates that there is still potential for 73.8% of variables not used in this study. So for further research it is recommended to explore more deeply related variables that can affect profitability such as Net Profit Margin, Total Asset Turnover, etc.

Research Contribution

This research is expected to add insight and knowledge regarding the factors that affect the profitability of cosmetic companies on the Indonesia Stock Exchange and is also expected as a means of developing knowledge, especially in the field of financial accounting which is theoretically studied in lectures. For companies, the research results are expected to be used as material for management consideration so that the company can determine strategies to maintain the desired profitability of the Company. For investors, it can be input material to obtain certainty of the rate of return on the investment made.

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