

Local Politics Influenced Performance For Local Companies? : A Story From Surabaya

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Abstract

The purpose of this research is to determine the differences of financial performance and market performance before, as at, and after direct election for local government executive on 2015. This research picks 30 Surabaya based listed companies as samples based on purposive sampling method with several criteria during 2014-2016. Method of hypothesis testing uses multivariate analysis of variance (manova) and analysis of variance (anova) test with three groups of periods, which are before, as at, and after the direct election for local government executive on 2015. The results show that there is no significant financial performance of local based company in Surabaya caused by direct local government election on 2015 measured by current ratio, working capital turnover ratio, debt to equity ratio and return to equity ratio. The market performance test also shows that there is no significant market performance of local based company in Surabaya caused by direct local government election on 2015 measured by abnormal return. Investors are advised to be more focus on the company's financial performance.

Keywords: financial performance; market performance; direct election; indonesia stock exchange.

Abstrak

Tujuan dari penelitian ini adalah untuk mengetahui perbedaan kinerja keuangan dan kinerja pasar sebelum, pada saat, dan setelah pemilihan kepala daerah langsung tahun 2015. Penelitian ini mengambil 30 perusahaan terbuka yang berbasis di Surabaya sebagai sampel berdasarkan metode purposive sampling dengan beberapa kriteria. selama 2014-2016. Metode pengujian hipotesis menggunakan analisis multivariat analisis varians (manova) dan analisis variansi (anova) dengan tiga kelompok periode yaitu sebelum, saat, dan sesudah pemilihan kepala daerah langsung tahun 2015. Hasil penelitian menunjukkan bahwa terdapat tidak signifikannya kinerja keuangan BUMD di Surabaya yang disebabkan oleh pemilihan kepala daerah secara langsung pada tahun 2015 yang diukur dengan rasio lancar, rasio perputaran modal kerja, rasio utang terhadap ekuitas dan rasio pengembalian terhadap ekuitas. Uji kinerja pasar juga menunjukkan bahwa tidak ada kinerja pasar yang signifikan dari perusahaan berbasis lokal di Surabaya yang disebabkan oleh pemilihan kepala daerah langsung pada tahun 2015 diukur dengan abnormal return. Investor disarankan untuk lebih fokus pada kinerja keuangan perusahaan.

Kata Kunci: Kinerja Keuangan, Kinerja Pasar, Pemilihan Langsung, Bursa Efek Indonesia

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INTRODUCTION

Politics is always an interesting topic to be followed. According to Holt (2007), there is a tense relationship between Indonesian political institution and cultural and economic framework. According to Suryadinata (2002), Indonesia politics can be interpreted on elections. Since 1999, general election in Indonesia and presidential election following it are significant events in the history of country. Indonesia is a portrait of democracy for another country.

Indonesia has several provinces. East Java is one of the prominent provinces in Indonesia. According to Statistic Central Bureau (2016), East Java contributed to 14,5% Regional Gross Domestic Product for Indonesia on 2015. It is only slightly below the highest contributor province, DKI Jakarta which is 17,02%. It means that East Java is one of the most important economic drivers for Indonesia. The capital city and also the largest city of East Java is Surabaya. Surabaya is one of the most historic cities in Indonesia. According to Dick (2003), in the nineteenth century, when Eastern Java was the frontier of an expanding plantation economy, Surabaya, with its natural harbor became the larger city. According to East Java Economic Administration Bureau (2015), the highest investment realization (domestic and foreign companies) in East Java is located in Surabaya which is 18,04 trillion rupiahs or 26,56% of all investment made in East Java on 2015. It figures how important Surabaya role for East Java and generally for Indonesia.

Since regulation about direct election for local government executive has been implemented on 2005, Surabaya has performed three times mayor elections which are on 2005, 2010, and 2015. Election on 2005 is won by Bambang D.H as the Surabaya city mayor. Election on 2010 is won by Tri Rismaharini, and she was elected again on 2015. On election

2015, Tri Rismaharini had a convincing win with high margin over 70% against her opponent, former Provincial Secretary of East Java, Rasiyo.

According to Berman and Haque (2015), Surabaya received many achievements and awards nationally and internationally under the Tri Rismaharini's leadership, for example the program creation of Garbage Bank to educate people to sort their garbage, creation of Green Village, creation of so many city's forests, Bungkul Park awards acquisition from the Asian Townscape Sector Awards from the United Nations Habitat Regional Office for Asia Pacific, Adiwiyata Mandiri award for several schools in Surabaya, creation Citizen Centered Service, highest score for Anti Corruption Initiative Assessment on 2011, ASEAN Environmentally Sustainable City Award 2012 and many other achievements. According to Giap *et. al.* (2015), Tri Rismaharini introduced a new online system to improve public service delivery and to ensure good and clean governance.

According to Ardison (2015), Tri Rismaharini is awarded as the third best mayor (second runner up) in the world for year 2014 by *citymajors.com*. She is also mentioned on Indonesia Forbes Magazine as one of ten women who inspire the nation on 2013. On February 2015, she is included into the top 50 of the best leaders in the world by *Fortune.com*. Based on those facts, Tri Rismaharini is the society's expected figure to lead Surabaya to be a better city.

One of the most highlighted achievements of Tri Rismaharini's leadership on Surabaya is on the economic sector. According to Surabaya Central Statistic Bureau (2016), under Tri Rismaharini leadership, Surabaya enjoyed economic growth on average of 7,16% on last six years. The number of Surabaya's economic growth is consistently above the national economic growth. The inflation

rate is also under controlled with average on 6,37% on last six years It shows that Tri Rismaharini succeed to lead Surabaya into a better welfare. Higher economic growth should be also enjoyed by the company that is mainly operated in Surabaya and surroundings. With higher economic growth, the local based companies will have greater opportunity to increase their financial and market performance.

If the local leader can influence the local economic circumstances, the direct election in Surabaya should influence performance of Surabaya and surroundings based companies, both in financial and market performance. Thus, there should be significant difference of local based company's financial and market performance. Especially, because of their favorite leader, Tri Rismaharini won the elections both in 2010 and 2015, it is argued that the local based company's financial and market performance increased. This research focuses to discuss on this issue.

Previous studies exhibit various findings about influence of politic events to economic context. According to Niederhoffer *et. al.* (1970), the short term market movements are intimately related to Presidential elections in United States of America. They are also related to other political events. Furthermore, there are no systematic differences in the performance of the market during Republican and Democratic administrations.

According to Ioannidis and Thompson (1986), a time series analysis did not reveal any statistically significant general relationship between opinion poll movements and the markets. But the result supports that the stock market prefers Conservative administration and respond positively to information that indicates the winning of Tories re-election. Privilege access to the information could lead investors to earn abnormal financial return,

if it is used selectively during election period. According to Forsythe *et. al.* (1992), even in nontraditional market, such as presidential stock market, interaction through the market structure produces correct prices. Furthermore, the availability of polling information on presidential election had little effect on market prices. It supports that Hayek hypothesis is robust. According to Leblang and Mukherjee (2004), anticipation of Democratic victory decreases stock price volatility. Furthermore, The GARCH and EGARCH models provide more accurate forecasts of stock volatility than the Marko switching models. According to Fuss and Bechtel (2008), only German small company's performance was positively linked with the probability of a right leaning coalition winning the election on the 2002 German federal election. The middle and large sized companies were not systematically linked with expected government partisanship. It may because the larger companies had already diversified their political risk, so they were no longer vulnerable to national government changes. The small companies was different, increasing electoral prospects of right leaning coalition caused volatility increases. The volatility models support the rational partisan hypotheses.

According to Goldman (2009), following the winning announcement of Republican, the return difference between companies that are classified as having a Republican linked board and those are classified as having Democratic board is positive. But, the announcement returns are positive for the Republican linked board companies and negative for Democratic linked board companies. Another result shows that there is positive and significant stock price on the announcement of board nomination of a politically connected individual.

Politics and Economic Relation

According to Caporaso and Levine (1992), there are three important traditions of politics. They are politics as government, politics as public life, and politics as the authoritative allocation of values. Politics and economics are methods of allocation regarding scarce resources. Unlike economics, which emphasizes on voluntary exchanges, the political system allocates resources using authority. According to Fahrholz (2007), political decision making and economic formation are highly interrelated. Political and economic system of society is marked by self organizing principle. The organizations determine elements and relations of those systems.

According to Gilpin and Gilpin (2001), the social or political purpose of economic activities is to achieve allocation of productive resources and the distribution of national product. In every society, the goals of economic activities and the role of markets in achieving those goals are determined by political process and

ultimately are responsibilities delegated by society to state. The market and economic factors do impose limits on what states can achieve.

Financial Performance

Financial performance is defined using financial ratio. According to Robinson *et. al.* (2004), ratio analysis is useful in comparing a company's performance to itself over time or to other companies. Thus, ratio analysis can be time series analysis and cross sectional analysis. Categories of ratio analysis are activity ratio, liquidity ratio, solvency ratio, profitability ratio, cash flow ratio, and price multiples ratio. This research uses liquidity ratio, activity ratio, solvency ratio, and profitability ratio. These ratios address particular aspects to company's operations, investments, financing, and profitability. The financial ratios used in this research are presented on table 2 below.

Table 1. Financial Ratio Formula

Financial Ratio	Formula
Liquidity Ratio	Current ratio = $\frac{\text{current assets}}{\text{current liabilities}}$
Activity Ratio	Working Capital Turnover Ratio = $\frac{\text{current assets} - \text{current liabilities}}{\text{sales}}$
Solvency Ratio	Debt to Equity Ratio = $\frac{\text{total debts}}{\text{total equity}}$
Profitability Ratio	Return to Equity = $\frac{\text{net income}}{\text{total equity}}$

Robinson *et. al.* (2004)

MARKET PERFORMANCE

Market performance is defined as abnormal return. According to Rani *et. al.* (2016), the abnormal return is the differences between the actual return and the expected return on a particular day. The equation of abnormal return is as follow.

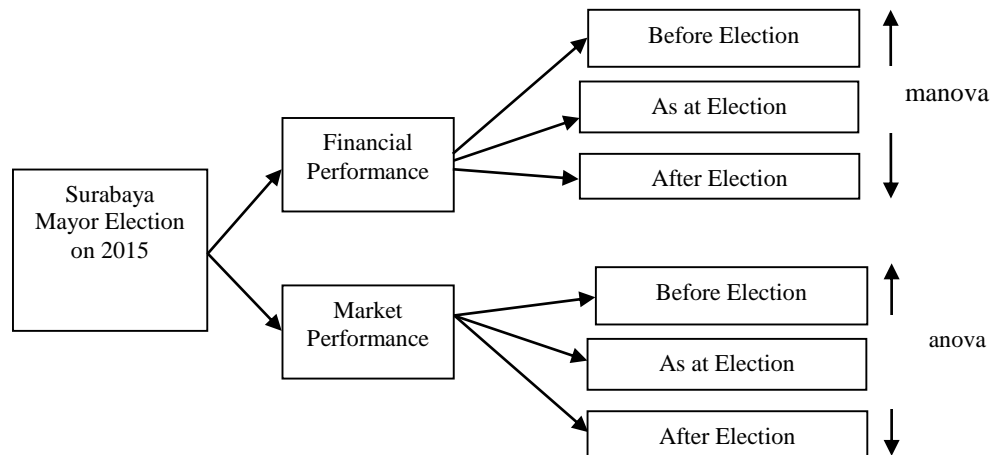
$$AR_{jt} = R_{jt} - E(R_{jt})$$

AR_{jt} = abnormal return of *j*th stock

R_{jt} = actual return in the event period.

$E(R_{jt})$ = normal or expected returns.

Figure 1. Theoretical Framework



Based from the literature reviews, two hypotheses were formulated on this research.

H_1 : There is significant difference of local based company's current ratio, working capital turnover ratio, debt to equity and return to equity ratio before, as at, and after direct election for local government executive on 2015.

H_2 : There is significant difference of local based company's abnormal return before, as at, and after direct election for local government executive on 2015.

METHOD

This research used financial report and stock trading report of Indonesia Stock Exchange listed companies which is headquartered or mainly operated in Surabaya as samples using purposive sampling method. This research set the following criteria for samples:

- Companies which have published financial report before, as at, and after direct election for local government executive on 2015.
- Companies which have had complete stock trade report before, as at, and after direct election for local government executive on 2015.

- Excludable for companies come from banking industry, because banking industry has different financial ratios to measure their performance.

Based on those criteria, 30 public companies are picked as samples.

This research uses secondary data which is acquired from Indonesia Capital Market Directory, company's financial report, company's annual report, and yahoo finance.

This research uses statistic analysis method. H_1 argue that there is significant difference of local based company's current ratio, working capital turnover ratio, debt to equity and return to equity ratio before, as at, and after direct election for local government executive on 2015. The difference of these three periods of financial ratios is tested using multivariate analysis of variance (manova). Manova is considered as an appropriate method because the research compares four groups of financial ratio variable and three groups of period variable. Manova needs several precondition tests, such as: normality test, separate variance homogeneity test, and simultaneously variance homogeneity test in order to

make sure that the model meet several manova assumptions.

H₂ is tested using analysis of variance (anova) because H₂ compares three period

groups. Anova needs precondition test, which is variance homogeneity test. The research's analysis methods are listed on table 2.

Table 2.

Hypotheses	Method	Precondition test	Type of test	Precondition test decision making	Hypotheses test decision making
H ₁	MANOVA	Normality	Kolmogorov Smirnov	<ul style="list-style-type: none"> • sig. > 0,05 ; normal distribution. • sig. < 0,05 ; abnormal distribution. 	<ul style="list-style-type: none"> • sig. < 0,05 then H₀ is rejected. • sig > 0,05 then H₀ is accepted.
			Levene Test	<ul style="list-style-type: none"> • sig. > 0,05 ; equal variance. • sig. < 0,05 ; unequal variance. 	
			Box's M Test	<ul style="list-style-type: none"> • sig. > 0,05 ; equal covariance matrix • sig. < 0,05 ; unequal covariance matrix 	
H ₂	ANOVA	Variance homogeneity test	Levene Test	<ul style="list-style-type: none"> • sig. > 0,05 ; equal variance. • sig. < 0,05 ; unequal variance. 	<ul style="list-style-type: none"> • sig. < 0,05 then H₀ is rejected. • sig > 0,05 then H₀ is accepted.

RESULT ANDF DISCUSSION

Precondition test results for manova analysis model are provided below.

Table 3. Precondition Test Results

Hypotheses	Method	Type of Test	Result	Explanation
H ₁	MANOVA	Kolmogorov Smirnov		
		CR	0.000	Abnormal distribution
		WCTO	0.000	Abnormal distribution
		DER	0.000	Abnormal distribution

Hypotheses	Method	Type of Test	Result	Explanation
		ROE	0.000	Abnormal distribution
		Levene Test		
		CR	0.927	Homogeneous variance
		WCTO	0.381	Homogeneous variance
		DER	0.426	Homogeneous variance
		ROE	0.433	Homogeneous variance
		Box's M Test	0.000	Heterogeneous variance
H ₂	ANOVA	Levene Test	0.374	Homogeneous variance

Source: Data processing.

Precondition test results of manova analysis model show that the model has equal variance with unequal covariance matrix. According to Gozali (2011), manova analysis model is still robust to be tested, although precondition test results

are failed to fulfill normality and variance homogeneity assumptions. Precondition test results of anova analysis model (second hypothesis) show that the model has homogeneous (equal) variance. So, the anova analysis model for second hypothesis is valid.

MANOVA ANALYSIS

H₁ is tested using multivariate analysis of variance. The results are provided on table 4.

Table 4. MANOVA Analysis Results

Effect	Value	F	Sig.	Explanation
Pillai's Trace	0.047	0.507	0.850	H ₀ is accepted
Wilks' Lambda	0.954	0.505	0.851	H ₀ is accepted
Hotelling's Trace	0.049	0.504	0.852	H ₀ is accepted
Roy's Largest Root	0.045	0.962	0.433	H ₀ is accepted
Test of Between Subjects				
CR	-	0.013	0.987	H ₀ is accepted
WCTO	-	0.206	0.814	H ₀ is accepted
DER	-	0.136	0.873	H ₀ is accepted
ROE	-	1.867	0.161	H ₀ is accepted

Source: Data processing.

Multivariate analysis of variance results show that H₀ is accepted. It means that there is no significant difference of company's current ratio, working capital turnover ratio, debt to equity and return on equity ratio before, as at, and after the direct election for local government executive on 2015. Furthermore, test of between subjects reveal that there is no

significant difference from each variables compared on the first hypothesis. These results reveal that direct election for local government executive on 2015 did not result to any significant difference on company's financial performance, including current ratio, working capital turnover ratio, debt to equity and return on equity ratio.

ANOVA ANALYSIS

H₂ is tested using analysis of variance (anova). The results are provided on table 5.

Table 5. ANOVA Analysis Results

	Mean Square	F	Sig.
Between Groups	1024.036	0.329	0.721
Within Groups	135438.384		

Source: Data processing.

Analysis of variance results show that sig. value is greater than significant level ($\alpha = 0,05$), then H₀ is accepted. It means that there is no significant difference of company's abnormal return before, as at, and after direct election for local

government executive on 2015. These results reveal that even the most favorite and the best mayor in Surabaya did not make any significant difference on company's market performance.

The Effect of Direct Election For Local Government Executive To Financial Performance of Local Based Company

Data analysis on this research shows that there is no significant financial performance of local based company in Surabaya caused by direct local government election on 2015 measured by current ratio, working capital turnover ratio, debt to equity and return to equity ratio. This finding is different with Fuss and Bechtel (2008) found that small company's performance was positively linked with federal election. The middle and large sized companies were not systematically linked with expected government partisanship because they had already diversified their political risk. On Surabaya case, even local company's performance had not linked with the local direct election.

It is argued that most of listed companies which are headquartered on Surabaya had their market not only in Indonesia, but on nation wide, moreover on international wide for several companies. So, the better local economy condition is not a warranty that the company can earn better financial performance. The national politics effect may influence company's financial performance. But the local politics was not necessarily influencing the local company's financial performance due to limited political impact. It is also argued that the incumbent mayor who won the election did not change her policy significantly, so there was no economic surprise on Surabaya. As the elected mayor could continue her prior policy, the company's performance at all was not influenced too much. Moreover, the elected mayor supported development of small and medium enterprises in Surabaya. So, there was no benefit can be earned by the big company just like company which is listed on Indonesia Stock Exchange. This condition had been anticipated by the company based on the previous leading experience of the elected mayor. There was no significant policy

change that can affect company's strategy at all.

The Effect of Direct Election For Local Government Executive To Market Performance of Local Based Company

This research find that there is no significant difference of company's abnormal return before, as at, and after direct election for local government executive on 2015. This finding is different with the previous research conducted by Ioannidis and Thompson (1986) that investors can earn abnormal return utilizing information provided on the election period selectively. On Surabaya case, the investors can not earn abnormal return since there was no different abnormal return identified on the election period.

This research is in line with Forsythe *et. al.* (1992), that political information provided on election period had little effect on market prices. There was no effect on Surabaya case. It is argued that the market had anticipated Surabaya's direct election result on 2015. The election on 2015 was won by the incumbent with more than 80% vote. This result was anticipated because the competition was not tight. Moreover, there was no candidate who had popularity equal with the incumbent candidate. Since the incumbent was too strong to be beaten, so the election result can be easily predicted.

Market's anticipation made no different on company's market performance. The company's share price was not affected much by the local election event. As long as the election process happened safely without any chaos, share performance was still in line with the market's expectation. The fact that there was no difference on company's financial performance also can be a reason why there was no difference on company's market performance. Investor's focus was on the company's financial performance.

Political events are proved by several researches to influence the economic condition, including company's performance.

But, Surabaya election on 2015 had different finding. Data analysis on this research shows that there is no significant financial performance of local based company in Surabaya caused by direct local government election on 2015 measured by current ratio, working capital turnover ratio, debt to equity and return to equity ratio. It is also argued that the incumbent mayor who won the election did not change her policy significantly, so there was no economic surprise on Surabaya. This condition also had been anticipated by the company based on the previous leading experience of the elected mayor. There was no significant policy change that can affect company's strategy at all.

Similar with the financial performance test result, data analysis shows that there is no significant difference of company's abnormal return before, as at, and after direct election for local government executive on 2015. It is argued that the market had anticipated Surabaya's direct election result on 2015 due to the competition which was not tight. As long as the election process happened safely without any chaos, share performance was still in line with the market's expectation.

Based on these findings, the investors are advised to be more selective on taking investment decision on election period. On certain case, it is possible that the market can not be influenced by political issue. Investors should look on the company's financial performance, especially because the financial performance itself was not influenced by the local political event. The effort to earn abnormal return may be useless on certain case. The future research may examine the other local region direct election's effect on the company's performance.

CONCLUSION

Political events are proved by several researches to influence the economic condition, including company's performance. But, Surabaya election on 2015 had different finding. Data analysis on this research shows

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