How liquidity and solvency affect stock prices. Does profitability really matter? Evidence from Indonesia

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ABSTRACT
The purpose of this study is to investigate the relationship between the variables shown in the conceptual model, with an emphasis on the role that profitability plays as a mediator in the relationship between stock prices, liquidity, and solvency. Secondary data from financial statements and stock summaries of businesses listed on the IDX are used in this quantitative research project. According to the findings, profitability and solvency both had a significant impact on stock prices, but liquidity had no appreciable effect.

Keywords:
Liquidity
Profitability
Solvency
Stock Price

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1. INTRODUCTION
Long-term financial instruments are traded on the capital market, which has the potential to greatly boost economic expansion and development. The capital market is essential to society as a whole and to businesses as a source of funding for investments. One of the most often used investment instruments in the capital market is shares. "High risk, high return" is a notion that guides share investments. An investor will take on greater risk in proportion to the reward they receive. Stock values are supposed to move steadily, according to investors, and they usually do so over time. Nonetheless, because share prices are set by the law of supply and demand, they frequently vary. Investors are exposed to risk when share values fluctuate, thus it is essential.

Long-term financial instruments are traded on the capital market, which has the potential to greatly boost economic expansion and development. The capital market is essential to businesses as a source of funding and to society overall. Because the building construction sub-sector is one of the cornerstone sub-sectors with enough potential to support Indonesia's economic growth, the focus of this research is the companies in this sub-sector that are listed on the Indonesia Stock Exchange for the period of 2013 to 2019. In terms of contributing to economic growth in Indonesia, the building industry comes in third. In order to reduce risk and forecast future earnings, investors must examine the variables that affect a company's share price.

Investors who wish to reduce risk and forecast returns must examine the variables that affect a company's share price.

A company’s share price can be used to gauge how well its management is doing. When a company's share price consistently
rises, investors will conclude that the business is well managed. One common belief is that share prices are a good indicator of a company's performance. The significance of a company's performance lies in its ability to serve as a gauge for its level of development [1].

One element that may have an impact on a company's share price is its financial performance. When making capital market investments, investors require information regarding the company's financial performance. Investors can forecast the company's future prospects, the prices and prospects of the securities, the amount of profit from capital invested, and other potentially useful information by understanding the financial health of the company [2].

Company management usually has better knowledge of the business's current state and future prospects, according to the signaling theory, which maintains that businesses must disclose information to investors in the shape of accounts statements, which can act as a guide for them regarding the state and prospects of the business. ahead of. By giving signals in the form of information, managers can reduce information asymmetry, according to signaling theory. Investors need precise, comprehensive, timely, and relevant analytical tools in order to make well-informed judgments about purchasing stocks. Investors will see the company's information as a clue that could influence the company's share price. Financial reports from companies are analyzed, and ratios including the profitability, solvency, and liquidity ratios are looked at.

Liquidity ratios are used to assess a company's ability to pay down short-term debt. A liquid company will have an easier time fulfilling its short-term obligations, which will help investors assess its performance positively. According to [2], investors place a larger value on a company's performance assessment when its share price rises.

The solvency ratio of a business indicates its capacity to settle all of its debt, both short- and long-term. Solvency has the potential to influence share prices because it influences investor interest. According to [3], the company's capacity to meet its financial commitments may draw in investors and boost the market demand for its shares. Profitability ratios indicate the extent to which a business can generate revenue. Increased profitability attracts the attention of investors and is a positive indicator. When there is significant investor interest in a firm's shares, the share price of the company will increase [4].

Previous studies and signal theory both suggest that financial ratios affect stock prices. Several research works have been carried out regarding do solvency and liquidity affect stock prices. However, research gaps indicate that there are still differences in the study results. The Current Ratio has a major impact on stock prices, according to research by [5]–[7]. On the other side, conflicting results were reported by [8]–[10] in their research, which denied that the current ratio had any bearing on share prices. Then, research by Amanah et al. from 2014 shows that the Quick Ratio has a significant influence on stock prices. The results of Penelitian [8], [11], on the other hand, show that the Quick Ratio has no effect on stock prices.

Studies conducted in 2015 and 2018 by [12]. demonstrate how the asset ratio significantly lowers stock prices, whereas studies conducted in 2018 show that the debt to asset ratio has a strong beneficial impact on stock prices. Following that, [13] research revealed that the Long Term Debt to Equity Ratio significantly and favorably influences stock prices. [12] offered other results, concluding that no meaningful correlation existed between share prices and the Long Term Debt to Equity Ratio.

The decline in share prices of enterprises in the building construction sub-sector between 2013 and 2019 and the uneven findings of studies based on business phenomena and research gaps were the issues. The research problem is resolved by signal theory because it has to do with how businesses provide information that can alert
investors to a company’s current state and future potential. Investors may use this information to help them decide whether or not to put money into the firm in question.

It is nevertheless necessary to view the degree of liquidity and solvency as positive information that can raise share values. These factors are not regarded by the market as information that can affect share prices. This is evident from the inconsistent research results. From the standpoint of signaling theory, when a corporation can use liquidity and solvency to boost its profitability, those factors can be viewed as positive signals. A company’s capacity to generate profits indicates that its prospects are improving, which encourages investors to purchase further shares. Positive comments from investors will cause the company’s share price to increase on the capital market. Because rising profitability will boost investor trust and interest in investing in the company, liquidity and solvency can therefore be favorable indicators when both can promote profitability.

2. LITERATURE REVIEW

2.1 Signalling Theory

In 1973, Spence made the first proposal for the theory of signaling. As the owner of the information, the sender tries to employ signals or cues to convey relevant information so that the recipient can utilize it. The recipient then modifies their behavior to fit their interpretation of the signal. Additionally, Ross (1977) created the signaling theory, which argues that CEOs are encouraged to reveal more information about their firm with potential investors in order to raise share prices since they have superior knowledge about it [4].

Information that investors must weigh in order to determine whether or not to purchase firm shares is signaled, according to signaling theory. Information availability is closely related to signaling theory in general. According to the signaling hypothesis, businesses must provide timely, accurate, comprehensive, and relevant financial disclosures to external parties. These financial reports can be used as an analytical tool for investment decision-making because they provide a comprehensive insight into the financial performance of the business in the past, present, and even future [14].

Firm internal parties release financial reports to inform investors about their business’s success, which is intended to draw investors to make investments in the firm, in accordance with the signaling theory previously described. To assess financial reports, one can utilize financial ratios, including those for activity, markets, profitability, liquidity, solvency, and profitability. Judging from the analysis of the financial report results, assume the business has performed successfully. Then, in order to raise the firm’s share price on the capital market, investors will be eager to purchase company stock.

2.2 Stock Price

Share price, or the cost of a share in the capital market at a given time depends on the supply and demand among market participants, claims [15]. Before choosing to purchase stock in a company, investors should carefully analyze a number of factors, according to [16]. Examining the company’s financial reports is one method, known as financial ratio analysis. The closing stock price of every company is used to calculate the stock price variable.

2.3 Liquidity

A measure of a company’s ability to settle short-term debt is called a liquidity ratio [17]. In this study, the following liquidity metrics were used:

1. The Current Ratio (CR) calculates how much It is possible for a firm to pay off its current liabilities...
with its available current assets. According to [17], the formula that follows can be utilized to calculate the current ratio:

\[
\text{Current Ratio} = \frac{\text{current liabilities}}{\text{current assets}}
\]

2. Utilizing the cash ratio, one can determine the amount of cash available to pay down short-term debt. As to [17], the Cash Ratio can be computed using the accompanying formula:

\[
\text{Cash Ratio} = \frac{\text{cash and cash equivalents}}{\text{current liabilities}}
\]

3. A ratio called the Quick Ratio (QR) shows how well a corporation can pay off its current debts with its current assets without accounting for inventory value. Being the least liquid component of current assets, inventories take longer to cash. According to [17], one can compute the Quick Ratio using the following formula:

\[
\text{Quick Ratio} = \frac{\text{current assets} - \text{inventory}}{\text{current liabilities}}
\]

2.4 Solvency

The amount of debt financing an organization’s assets is measured by a ratio known as solvency. The solvency ratio, according to [17], is a general indicator of a company’s ability to pay off all of its short- and long-term debts in the case of a liquidation. The following solvency metrics were used in this investigation:

1. Debt to Asset Ratio (DAR) is a ratio used to measure how much a company’s assets are financed by debt or how much the company’s debt affects asset management. According to Kasmir (2015), DAR can be measured using the following formula:

\[
\text{DAR} = \frac{\text{total debt}}{\text{total assets}}
\]

2. Long Term Debt to Equity Ratio (LTDER) is the ratio between long-term debt and own capital. LTDER measures how much of each rupiah of its capital is used as collateral for long-term debt by comparing long-term debt with the capital provided by the company [17]. According to [17], LTDER can be calculated using the subsequent formula:

\[
\text{LTDER} = \frac{\text{long term debt}}{\text{total equity}}
\]

2.5 Profitability

According to Kasmir (2015), profitability is a ratio that reflects how much a business can make. The following metrics were employed in this study to determine profitability:

1. An organization’s capacity to turn a profit on all of its assets is gauged by its return on assets, or ROA, ratio. The formula below can be used to compute ROA, per [17]:

\[
\text{ROA} = \frac{\text{net profit after tax}}{\text{total assets}}
\]

2. A company’s ability to manage investor funds to generate net profits is measured by a ratio called return on equity, or ROE. According to [17], the following formula can be used to calculate ROE:

\[
\text{ROE} = \frac{\text{net profit after tax}}{\text{total equity}}
\]
2.6 Hypothesis Development

![Research Model Diagram]

Figure 1. Research Model

<table>
<thead>
<tr>
<th>Hypothesis</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>H1</td>
<td>The price of the stock will increase in direct proportion to its liquidity</td>
</tr>
<tr>
<td>H2</td>
<td>The share price increases with increasing solveability</td>
</tr>
<tr>
<td>H3</td>
<td>The share price increases in proportion to the profitability</td>
</tr>
<tr>
<td>H4</td>
<td>The profitability increases with more liquidity</td>
</tr>
<tr>
<td>H5</td>
<td>The profitability increases with the degree of solvability</td>
</tr>
<tr>
<td>H6</td>
<td>The relationship between liquidity and stock prices can be mediated by profitability</td>
</tr>
<tr>
<td>H7</td>
<td>The relationship between liquidity and stock prices can be mediated by profitability</td>
</tr>
</tbody>
</table>

3. RESEARCH METHODS

Secondary data sources are consulted in this research. A overview of shares and financial reports of building construction subsector companies listed on the Indonesia Stock Exchange (BEI) for the years 2017 through 2022 can be accessed through the data source’s website, www.idx.co.id. Additional resources of assistance include news stories, magazines, and these companies’ websites.

Twelve businesses in the building construction subsector that are listed on the IDX for the years 2017 through 2022 make up the research population. Samples are among the characteristics of the population that researchers use, according to [18]. In order to obtain non-probability sample data, this study uses saturation sampling. Saturated sampling, a sampling method, is utilized when the entire population serves as the sample. The observation sample, which consisted of 12 companies in the building construction subsector employed in this study, comprised 84 enterprises in total across the 6-year observation period.

Structural equation modeling, or SEM, is the analysis technique employed in this work. When certain issues with the data arise, such as a limited study sample size, missing data (missing values), and multicollinearity, the partial least squares, variant-based SEM statistical approach is intended to achieve multiple regression. Partial least squares are useful for all data scales and small sample sizes.

4. RESULTS AND DISCUSSION

4.1 Results

1. Descriptive Statistical Analysis

Values of the mean, median, maximum, minimum, and standard deviation are examples of data that are described by descriptive statistics [19].
Table 1. Descriptive Statistics Results

<table>
<thead>
<tr>
<th></th>
<th>Mean</th>
<th>Median</th>
<th>Min</th>
<th>Max</th>
<th>Standard Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>CR</td>
<td>149,023</td>
<td>140,324</td>
<td>67,455</td>
<td>313,949</td>
<td>44,200</td>
</tr>
<tr>
<td>Cash Ratio</td>
<td>32,914</td>
<td>32,604</td>
<td>0,774</td>
<td>99,082</td>
<td>20,563</td>
</tr>
<tr>
<td>QR</td>
<td>131,775</td>
<td>127,993</td>
<td>47,516</td>
<td>290,104</td>
<td>44,712</td>
</tr>
<tr>
<td>DAR</td>
<td>58,923</td>
<td>56,810</td>
<td>28,151</td>
<td>97,258</td>
<td>15,903</td>
</tr>
<tr>
<td>LTDER</td>
<td>41,040</td>
<td>23,968</td>
<td>2,814</td>
<td>277,141</td>
<td>46,556</td>
</tr>
<tr>
<td>ROA</td>
<td>1,489</td>
<td>2,898</td>
<td>-43,864</td>
<td>16,494</td>
<td>8,561</td>
</tr>
<tr>
<td>ROE</td>
<td>-4,605</td>
<td>8,809</td>
<td>-413,564</td>
<td>28,536</td>
<td>64,442</td>
</tr>
<tr>
<td>HS</td>
<td>1,099,917</td>
<td>840</td>
<td>50</td>
<td>3875</td>
<td>874,349</td>
</tr>
</tbody>
</table>

Source: Output SmartPLS Versi 3 (processed data)

Based on the computation results from 84 observation data points, as shown in the above table. Nusa Konstruksi Enjiring Tbk’s lowest (minimum) share price for the period of 2019 to 2021 is IDR 50. Meanwhile, PT. Pembangunan Perumahan (Persero) Tbk’s 2013 share price value reached its highest (maximum) of IDR 3,875 at that time. With a standard deviation of IDR 874,349 and an average share price value of IDR 1,099,917, the average value was found to be more significant than the standard deviation value. Because the average deviation distance is less than the average value of the variable, it demonstrates the low risk and fluctuation of the Share Price variable data during the research period.

In 2018, Waskita Karya (Persero) Tbk had the lowest (minimum) liquidity as measured by the Current Ratio (CR), with a value of 67.455%. In the meantime, Indonesia Pondasi Raya Tbk recorded the highest (maximum) Current Ratio (CR) figure in 2013 at 313.949 percent. The standard deviation of the current ratio (CR) is 44.200%, and its average value is 149.023%. Because the average deviation distance is smaller than the average value of the variable, it implies little risk and fluctuation in the Current Ratio (CR) variable data over the research period. This signifies that the average value is bigger than the standard deviation value.

Liquidity has the lowest (minimum) value of 0.774% for Indonesia Pondasi Raya Tbk in 2019, as measured by the Cash Ratio. At Indonesia Pondasi Raya Tbk 2013, the greatest (maximum) Cash Ratio value was 99.082%. The Cash Ratio has a standard deviation of 20.563% and an average value of 32.914%. Because the average deviation distance is smaller than the average value of the variable, it implies little risk and fluctuation in the cash ratio variable data over the study period. This signifies that the average value is bigger than the standard deviation value.

Liquidity had the lowest (minimum) value in 2017 at 47.516% in Bukaka Teknik Utama Tbk, as measured by the Quick Ratio (QR). In the meantime, Indonesia Pondasi Raya Tbk had the highest (maximum) Quick Ratio (QR) value in 2013 at 290.104%. The Quick Ratio has an average value of 131.775% and a standard deviation of 44.712%. Because the average deviation distance is smaller than the average value of the variable, it may be inferred that there was little risk and variation in the Quick Ratio variable data across the study period when the standard deviation value was greater than the average.

In Indonesia Pondasi Raya Tbk, solvency has the lowest (minimum) value of 28.151% in 2015, as measured by the Asset Ratio (DAR). In contrast, Acset Indonusa Tbk had the greatest (largest) asset
The debt to asset ratio (DAR) value in 2019 was 97.258%. The average value of the debt to asset ratio (DAR) is 58.923%, with a standard deviation of 15.903%. Because the average deviation distance is smaller than the average value of the variable, it can be inferred that there was little risk and fluctuation in the Asset Ratio (DAR) variable data during the research period. The average value is greater than the standard deviation value, as demonstrated by this.

Based on the Long Term Debt to Equity Ratio, Asset Indonusa Tbk's solvency had the lowest value in 2014. It was 2.814%. Meanwhile, with a maximum Long Term Debt to Equity Ratio of 277.141 percent in 2019, Waskita Karya (Persero) Tbk had the highest ratio of any company. The Long Term Debt to Equity Ratio (LTDER) has a mean value of 41.040% and a standard deviation of 46.556%.

Return on Assets (ROA) of 16.494% in 2015. Return on Assets (ROA) has an average standard deviation of 1.489%, or 8.561%. It may be deduced that there was significant risk and erratic fluctuations in the Return on Assets variable data during the course of the study because the average deviation distance is higher than the variable’s average value. The average value is less than the standard deviation number, which explains this.

When measured by Return on Equity (ROE), Asset Indonusa Tbk's profitability has the lowest (minimum) value of -413.564% in 2018. As an example, Bukaka Teknik Utama Tbk's maximum Return on Equity (ROE) of 28.536% in 2018 was the greatest. Return on equity has an average (mean) value of -4.605% and a standard deviation of 64.442%. It can be deduced that there was high risk and unstable oscillations in the Return on Equity (ROE) variable data during the research period when the average value was lower than the standard deviation value because the average deviation distance is bigger than the average value of the variable.

Table 2. R-Square Results

<table>
<thead>
<tr>
<th></th>
<th>R Square</th>
<th>R Square Adjusted</th>
</tr>
</thead>
<tbody>
<tr>
<td>Harga Saham</td>
<td>0.278</td>
<td>0.251</td>
</tr>
<tr>
<td>Profitabilitas</td>
<td>0.115</td>
<td>0.093</td>
</tr>
</tbody>
</table>

Source: Output SmartPLS Versi 3 (processed data)

The aforementioned table indicates that share prices have a value of 0.278, or 27.8%, indicating that the factors liquidity, solvency, and profitability have a 27.8% influence on share prices. In the meantime, factors not included in this study had an impact on the remaining 88.5%. Since the number is still greater than 0.1 or 10%, it is still possible to conduct additional tests in hypothesis testing even though it falls under the low correlation range.
b. Q-Square

In addition to evaluating the R-Square's magnitude, the Q-Square can be used to examine the PLS model. The model's observation values and parameter estimates are evaluated using Q-Square. The PLS blindfolding approach was used to perform the calculation, and the following outcomes were obtained:

Table 3. Q-Square Results

<table>
<thead>
<tr>
<th></th>
<th>SSO</th>
<th>SSE</th>
<th>Q2(=1-SSE/SSO)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Harga Saham</td>
<td>84,000</td>
<td>62,078</td>
<td>0,261</td>
</tr>
<tr>
<td>Likuiditas</td>
<td>252,000</td>
<td>252,000</td>
<td></td>
</tr>
<tr>
<td>Profitabilitas</td>
<td>168,000</td>
<td>153,937</td>
<td>0,084</td>
</tr>
<tr>
<td>Solvabilitas</td>
<td>168,000</td>
<td>168,000</td>
<td></td>
</tr>
</tbody>
</table>

*Source: Output SmartPLS Versi 3 (data processed)*

It is known that the value for share prices is 0,261 based on the above table. It can be inferred that liquidity and solvency have strong predictive importance for stock prices because the value is greater than zero. Profitability has a value of 0,084. It can be inferred that liquidity and solvency have predictive implications for profitability because the value is greater than zero.

c. Direct Effects

The direct effect test was carried out using the PLS bootstrapping technique with the following analysis results:

Table 4. Direct Effect Results

<table>
<thead>
<tr>
<th></th>
<th>Original Sample Mean</th>
<th>Sample Mean</th>
<th>Standard Deviation</th>
<th>T Statistics</th>
<th>P Values</th>
</tr>
</thead>
<tbody>
<tr>
<td>Likuiditas -&gt; Harga Saham</td>
<td>-0.003</td>
<td>-0.014</td>
<td>0.102</td>
<td>0.034</td>
<td>0.973</td>
</tr>
<tr>
<td>Likuiditas -&gt; Profitabilitas</td>
<td>0.265</td>
<td>0.280</td>
<td>0.111</td>
<td>2.384</td>
<td>0.017</td>
</tr>
<tr>
<td>Profitabilitas -&gt; Harga Saham</td>
<td>0.344</td>
<td>0.353</td>
<td>0.054</td>
<td>6.346</td>
<td>0.000</td>
</tr>
<tr>
<td>Solvabilitas -&gt; Harga Saham</td>
<td>0.501</td>
<td>0.505</td>
<td>0.084</td>
<td>5.939</td>
<td>0.000</td>
</tr>
<tr>
<td>Solvabilitas -&gt; Profitabilitas</td>
<td>-0.103</td>
<td>-0.089</td>
<td>0.142</td>
<td>0.726</td>
<td>0.468</td>
</tr>
</tbody>
</table>

*Source: Output SmartPLS Versi 3 (processed data)*

Based on the data processing presented in the table, the following results can be concluded:

Liquidity does not have a significant effect on share prices, this is shown by the t-statistic value (0.034) < 1.96 and the p-value (0.973) > 0.05. It means that it is accepted and rejected. Thus, hypothesis 1, which states that "The more liquid, the higher the share price," is rejected.

Solvency has a positive and significant effect on share prices, The original sample's parameter coefficient value of 0.501, the t-statistic (5.939) > 1.96, and the p-value (0.000) < 0.05 all support this. It implies that the share price will rise by IDR 0.501 for every 1 value added to solvency and vice versa. It indicates that it is both accepted and rejected. As a result, it is agreed upon that hypothesis 2, "The more solvable, the higher the share price," is true.

The parameter coefficient value (original sample) of 0.344, the t-statistic (6.346) > 1.96, and the p-value (0.000) < 0.05 all support the idea that profitability has a positive and significant impact on share prices. Consequently, for every unit increase in profitability of 1, the share price will increase by IDR 0.344, and vice versa. It denotes both acceptance and rejection. Therefore, it is acknowledged that hypothesis 3, which asserts that "The higher the profitability, the higher the share price," is true.
Liquidity has a positive and significant effect on profitability, the parameter coefficient value (original sample) of 0.265, the p-value (0.017) < 0.05, and the t-statistic (2.384) > 1.96 all support this. Based on this, an increase in liquidity of one value will lead to a 0.265 gain in profitability, and vice. It suggests that Ha is rejected while Ho is accepted. As a result, it is agreed upon that hypothesis 4, "The more liquid, the higher the profitability," is true.

Solvency does not have a significant effect on profitability, the t-statistic value (0.726) < 1.96 and the p-value (0.468) > 0.05 demonstrate this. This suggests that while H0 is accepted, Ha is denied. That means there is no evidence to support hypothesis 5, which states that the profitability increases with solvability.

d. Indirect Effect

By examining the outcomes of the particular indirect effects analysis, which are shown in the following table, indirect effects are calculated using the PLS bootstrapping technique:

<table>
<thead>
<tr>
<th>Table 5. Indirect Effect Results</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
</tr>
<tr>
<td><strong>Likuiditas → Profitabilitas → Harga Saham</strong></td>
</tr>
<tr>
<td>----------------------------------</td>
</tr>
<tr>
<td>0.091</td>
</tr>
<tr>
<td><strong>Solvabilitas → Profitabilitas → Harga Saham</strong></td>
</tr>
</tbody>
</table>

*Source: Output SmartPLS Versi 3 (processed data)*

Based on the data processing presented in the table, the following results can be concluded:

Profitability is able to mediate the relationship between liquidity and share prices, with a p-value of 0.023 < 0.05, it is demonstrated by the t-statistic value (2.282) > t-table value (19.96). When profitability strongly mediates liquidity on share prices, intervening is classified as total mediation in this scenario. The notion that "Profitability mediates the relationship between Liquidity and Share Prices" is so accepted.

The relationship between solvency and share prices cannot be mediated by profitability, The t-statistic value (0.685) < t-table value (1.96) and the p-value (0.494 > 0.05) demonstrate this. This means that hypothesis 7, which claims that "Profitability mediates the relationship between Solvency and Share Prices," is not supported.

4.2 Discussion

a. The Effect of Liquidity on Stock Prices

Liquidity has little effect on share prices, according to the data analysis's findings. According to this research, investors are not very concerned with a firm's liquidity level because it has little bearing on the share price of the company and its capacity to settle short-term debt. Consequently, investors should not use a company’s high or low degree of liquidity as a signal when deciding whether to put their money in it.

The findings of this study also contradict the signal hypothesis, which holds that when a company is liquid, investors may see this as a good indication because it will be simpler for the company to settle its immediate debts. In this manner, investors will view the business's financial performance favorably and become interested in funding it.

The findings of this study run counter to those of studies by [20]–
b. The Effect of Solvency on Stock Prices

Share prices are significantly and favorably impacted by solvency, per the data study. According to the study’s findings, if a company is making sensible profits, investors are inclined to ignore excessive debt levels. Moreover, investors see a large amount of debt as an indication of the company’s bright future and high degree of external confidence in its capacity to obtain loans. It might persuade financiers to invest in the company, boosting stock values [27].

The utilisation of debt by a company is interpreted by investors as an indication that the company is willing to take on risks in order to maximise profits, and this theory supports the findings of this study by arguing that a company’s solvency can influence their decisions about which stocks to buy. The company will eventually turn a profit and increase investors’ earnings per share if it can manage its debt well. However, the company must continue to be solvent since, in the end, investors will not take on the risk of the company’s continuing debt load if it is too large. The findings of this study are consistent with those of studies by [27]–[29], which stated that solvency has a positive and significant effect on stock prices.

c. The Effect of Profitability on Stock Prices

Profitability has a strong and favorable impact on share values, according to the data analysis results. The study’s conclusions show that a company’s profitability level draws investors to buy shares, which raises the stock’s value because it shows the company’s potential to generate significant profits for its owners [30]. On the other hand, a low degree of profitability can lower share prices since investors typically steer clear of investing in low-profit companies in an effort to limit losses or find more lucrative opportunities.

A signal theory, which contends that great profitability might be an indication of successful business performance and so entice investors to put money into the company in question, lends credence to the findings of this study. Due to the fact that investors essentially want to receive the highest possible return on their investment, the company’s ongoing profitability will boost potential investors’ interest and confidence in making an investment [31]. Consistent with the results of this study, research by Oleh [5], [8], [32] has shown that profitability has a significant and positive impact on share prices.

d. The Effect of Liquidity on Profitability

Based on data analysis, profitability is positively and strongly impacted by liquidity. Based on the study, a company’s liquidity boosts its ability to pay down short-term debt. When a firm has strong liquidity, it means that working capital is available for its operations. If the company’s operations are successful, then its activities will also be successful, supporting higher company profitability [33]. On the other side, if the company has insufficient liquidity, it may not have enough cash on hand to meet its short-term payments on schedule. The company’s capacity to meet its needs and run its operations efficiently may be hampered as a result, which could eventually damage its profitability. According to signal theory, which is supported by
the study’s findings, information about liquid companies might entice potential investors to invest in the company, which will ultimately boost profitability. The findings of this study are consistent with those of [33]–[36] studies, which showed that liquidity significantly and favorably affects profitability.

e. The Effect of Solvency on Profitability

The data analysis indicates that solvency has no discernible impact on profitability. The study’s findings demonstrate that there is no discernible relationship, either negative or positive, between a company’s solvency and profitability. However, low debt usage indicates that the company is funded primarily by internal funds rather than external funds, which will have an impact on increasing profitability because the company will bear lower debt costs [37]. In contrast, a higher proportion of debt used as company capital will result in increased debt costs and interest that the company must bear, thereby reducing the amount of profit earned by the company.

The findings of this study contradict the signal hypothesis, which holds that a company’s debt can be interpreted as an indication of its willingness to take calculated risks in order to maximize earnings. The findings of this study contradict those of studies by [36], [38], [39], which found a favorable and significant relationship between solvency and profitability. However, the results of this study are in line with those of [40], [41] studies, which also revealed no evidence of a connection between profitability and solvency.

f. The Effect of Profitability in Mediating the Relationship between Liquidity and Stock Prices

Profitability can mediate the relationship between liquidity and stock prices, according to the analysis of the data. The signaling theory, which argues that a corporation will find it simpler to meet its short-term debt payments on schedule when it is in a liquid condition, is supported by the research’s findings. It boosts the company’s earnings and facilitates efficient business operations. Investors will be encouraged by the company’s rising profitability. It is going to increase share demand. The price of the company’s shares will rise due to the strong demand for them.

The study’s conclusions demonstrate that, although a company’s liquidity may not necessarily translate into higher share prices, it can do so if it is accompanied by a rise in profitability. This is because high profitability can pique investors’ interest in making an investment in the company, which in turn raises share prices. Thus, as share prices rise, the profitability variable may have an effect on liquidity if it is included as a mediating variable.

g. The Effect of Profitability in Mediating the Relationship between Solvency and Stock Prices

An analysis of the data indicates that profitability is not able to mediate the relationship between solvency and stock prices. The study’s conclusions run counter to the signaling idea. From the standpoint of signal theory, debt can be interpreted as an indication of a company’s bravery in taking calculated risks to optimize profits. Profitability growth is a sign that a company’s prospects are improving, which will boost investor demand for the company’s shares and drive up the price of those shares on the capital market.

Businesses in the building construction subsector are primarily backed by debt, which lowers their profitability because of the high interest expenses they must pay. The more outside funding a firm uses for investment activities, the more
interest it must pay, which lowers the company's overall profitability. Since investors avoid purchasing stock in companies with low levels of profitability, the share price of the company declines. This decline in profitability is viewed as a false signal, or "lousy news." Therefore, it can be said that solvency in rising share prices is unaffected by the addition of the profitability variable as a mediating variable.

5. CONCLUSION

The following findings are drawn from the data analysis results and the presented discussion:

Since share prices are not significantly impacted by liquidity, H1 is rejected. These results suggest that while a company's ability to pay off short-term obligations has little effect on its share price, investors are not very concerned about a company's liquidity level. Therefore, a company's liquidity level—whether high or low—does not provide information that can help investors decide which stocks to buy. It is not information that investors may use as a guide when choosing which stocks to buy.

Solvency has a positive and significant effect on share prices, meaning that the more solvable, the higher the share price. So, H2 is accepted. The results of this research indicate that the level of company solvency can influence investors' stock investment decisions because investors consider the use of debt as favorable information, which indicates the company's courage in bearing risks to maximize the profits obtained. The price of the company's shares may rise as a result of encouraging investors to make investments.

Profitability has a positive and significant effect on share prices, meaning that the higher the profitability, the higher the share price. So, H3 is accepted. The results of this research indicate that high profitability can be a positive signal for investors since it suggests that the business is operating more efficiently, investors will be more inclined to purchase firm stock.

H4 is acceptable since liquidity significantly and favorably affects profitability. According to the research's findings, a company's capacity to settle its short-term debts increases with its liquidity. Where high liquidity reflects the availability of sufficient working capital to run the company's operations well and support increased company profitability.

Solvency does not have a significant effect on profitability, so H5 is rejected. The results of this research show that the level of company solvency does not significantly influence profitability, and there is a negative or opposite relationship. Where the use of a high proportion of debt can increase the cost of debt and interest, it will reduce the size of the company's profits. Alternatively, a company's profitability may rise if it uses less debt because of the lower interest costs and costs associated with debt.

Since profitability can act as a mediator in the relationship between share prices and liquidity, H6 is approved. According to the study's findings, a company's liquidity does not automatically translate into higher share prices. However, liquidity can raise share prices if it is coupled with a rise in profitability, as this might pique investors' interest in funding the business. The company's share price will rise as a result.

As a result, H7 is rejected since profitability cannot moderate the link between solvency and share prices. According to the study's findings, businesses that rely more heavily on debt financing would become less profitable as a result of the high interest expenses they must pay. Investors avoid purchasing shares in businesses with low levels of profitability because they view this drop in profitability as a false indicator.

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