



The Effect of Profitability on Stock Return (Study on Financial Technology Companies Listed on NASDAQ)

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Abstract. This study aims to obtain an overview of the profitability of stock return in financial technology companies listed on the NASDAQ. The type of research used is descriptive and verification research with explanatory research methods. The sampling technique in this study is purposive sampling technique with a total sample of 6. Financial technology companies listed on the NASDAQ are the objects in this study. The data analysis technique used in this study is a panel data regression analysis technique with data processing applications using the Eviews 12 program. This study obtained findings showing that profitability negatively affects stock return. Based on the results of this study, it can be concluded that when profitability (ROE) increases, stock return do not increase.

Keywords: Profitability · Stock Return · Financial Technology

1 Introduction

The capital market is one of the economic instruments that is growing very rapidly today. The capital market is used as an indicator of state progress that is able to support the country's economy as needed (Afrino & Erni, 2019) and provide direct benefits to the community. Therefore, the existence of the capital market is very important for companies and investors.

Companies that generate profits prove that the company can provide stock returns to investors, so potential investors will be interested in buying company shares, it can increase stock returns (Jasman & Kasran, 2017). As one of many forms of investment, stock returns are important to investors. Usually, investors will tend to invest their funds in stocks that are considered to have the potential to provide high returns and have good growth potential in the long run. Therefore, investors must be able to predict stock returns from their investments (Nugroho, 2020).

Stock return is an advantage given by the company to investors because of the courage to bear their investment risks (Saragih, 2018). The purpose of trading activities carried out by investors is to seek profits from buying and selling shares (Saragih, 2018).

Investors will consider two things, namely the expected return and risk in the investment. The better the company's performance, the less likely the investment risk will

be borne and the more likely the stock return will be obtained (Damanik, Sadalia, & Silalahi, 2019). Investing in company stocks must be chosen well because not all companies promise high stock returns (Malau, 2013). Therefore, the size of stock returns will affect investor interest in investing (Damanik et al., 2019).

Research on stock returns has been widely researched, because stock returns are one of the considerations (Damanik et al., 2019), investor interest and interest in investing in companies (Jasman & Kasran, 2017). Stock return research was first examined by (Fama & MacBeth, 1973) where the study aimed to examine the relationship between return (return) and risk on New York Stock Exchange stocks. Research discussing stock returns has been conducted in several companies, in the form of state-owned companies (Jasman & Kasran, 2017), banking companies (Devitra, 2011), manufacturing companies (Sari et al., 2018; N. Allozi et al., 2016), infrastructure companies (Malau, 2013), consumer goods industry (Sari et al., 2018), wholesale and retail trading companies (Saragih, 2018), coal mining companies (Damanik et al., 2019), and pharmaceutical industry (Anjani & Syarif, 2019).

In investment, the financial technology (Fintech) industry offers both benefits and risks. Investors have opportunities for high growth in this industry, but also have high risk opportunities (Goss, 2020). With the emergence of fintech companies as a new business sector, it has aroused interest from investors (Suprun, Petrishina, & Vasylichuk, 2020).

Based on data in Fig. 1 showing six FinTech companies on NASDAQ from 2013 to 2021, namely MarketAxess Holdings Inc (MKTX), Equifax Inc (EFX), SS&C Technologies Holdings Inc (SSNC), Envestnet Inc (ENV), Green Dot Corporation (GDOT), and Moodys Corporation (MCO). The data shows that the six companies experience fluctuations tend to decline every year. In assessing the performance of a company, investors need to analyze the company's finances. This can help investors decide whether the

Stock Return of 6 financial technology companies on NASDAQ

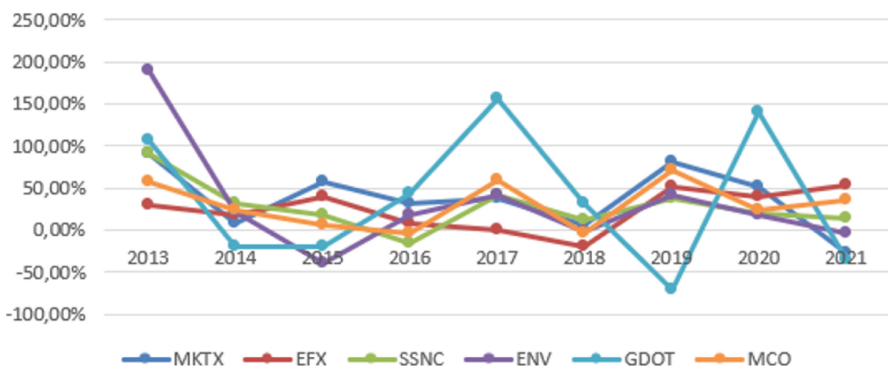


Fig. 1. Development of Stock Return of Financial Technology Sector Companies in 2013–2021

company's shares are worth buying. One way to analyze a company's financial performance is to analyze the company's financial ratios. Through financial ratios, investors can identify the weaknesses and strengths of a company. (Nalurita Febria, 2017).

The movement of stock returns can be influenced by various factors, namely excess market returns, small market capitalization (SMB) portfolios and book-to-market (HML) portfolios (Axel Melander Norinder, 2018), inflation (Ibrahim & Agbaje, 2013), Gross Profit Margin (GPM), Return on Assets (ROA), Return on Equity (ROE), and Earnings per Share (EPS) (Allozi & Obeidat, 2016), Current Ratio (Anjani & Syarif, 2019), interest rates and exchange rate changes (Ahmad, Rehman, & Raof, 2010), and liquidity (Akram, 2014).

Investors really like high income from each investment (Jasman & Kasran, 2017). Therefore, before investors invest their funds, investors need to analyze the company's condition so that they can predict the stock return to be achieved, by looking at several factors that can affect stock returns (Jasman & Kasran, 2017). The benchmark for investors in assessing a company is to look at the profitability of a company (Sugosha, 2017). Profitability is one of the important focuses for investors in making decisions to invest. If the company's profitability is high, investors will be more interested in investing the funds they have in a company, because it is considered that the company has a good ability to generate profits. In other words, investors will analyze the information provided by the company's management before making investment decisions as good signals or bad signals (Brigham & Houston, 2007). If the information is a good signal for investors, then the stock price will rise (Bertuah & Sakti, 2019), and the increase in the company's stock price will provide high returns for investors (Saragih, 2018).

In this study, Return On Equity (ROE) is used as a profitability indicator because ROE is one of the most important indicators used by investors to increase the value of profits in a company before investing, namely by knowing the amount of ROE in a company. ROE is a tool to measure a company's ability to generate profits using its own capital (Nurhikmawaty, Isnurhadi, Widiyanti, & Yuliani, 2020).

2 Methods

2.1 Research Design

This research was conducted to determine the effect of profitability on stock returns. The independent variable used in this study is profitability which is measured using Return On Equity while the dependent variable is stock return. The object of research taken in this study is financial technology companies listed on NASDAQ for the 2013–2021 period. This research was conducted in less than a year, from March 2022 to January 2023, so the data collection technique used in this study is explanatory research. The explanatory research method is carried out through collecting information by studying objects within a certain period of time in the long term with the aim of knowing whether variables are caused or influenced or not by other variables (Sugiyono, 2017).

2.2 Sample

Sampling is the process of selecting the right number of elements from a population, thus allowing research samples and understanding of traits or characteristics to generalize

these traits or characteristics to population elements (Sekaran & Bougie, 2016). The sampling technique that will be used in this study is *purposive sampling*. *Purposive sampling* techniques are chosen because of certain considerations such as limited time, energy and limited costs. With this technique, the sample is determined by researchers based on certain objectives, but has met the applicable terms and conditions.

2.3 Data Collection Technique

The data collection technique used by the authors in this study is a documentation technique. Documentation technique is a secondary data collection technique carried out by studying documents related to all data needed in this study. In carrying out this documentation method, researchers collect information about the financial statements of related *financial technology* companies.

2.4 Data Analysis Technique

This study uses descriptive analysis to describe research variables, including: 1) Descriptive Analysis of Variable X (Profitability), where variable X is focused on profitability research through Return on Equity (ROE); 2) Descriptive Analysis of Variable Y (Stock Return), where variable Y is focused on research on stock returns through stock prices (closing price). This study also uses verifiative analysis which is used to test hypotheses using statistical tests and focuses on revealing the behavior of research variables. The processing of this research data was carried out using panel linear regression analysis. Verifiative data analysis is used to determine the results of this study, namely profitability (ROE) which has an influence on stock returns. A linear regression model can be called a good model if it satisfies the classical assumptions of k statistics consisting of the assumptions of normality, autocorrelation, multicollinearity, and heteroscedasticity. According to (Widarjono, 2013), there are three kinds of analysis model approaches in panel data regression, namely common effect model (CEM), fixed effect model (FEM), and random effect model (REM). To determine the panel data regression model that is suitable for use, a chow-test, hausman test, langrage multiplier test is performed. The chow test is used to determine the common effect approach or fixed effect approach. While the Hausman test is used to determine between a fixed effect approach or a random effect approach (Widarjono, 2013). Uji Langrage Multiplier is used to determine the best model between the random effect model and the common effect model (Baltagi et al., 2012).

3 Result and Discussion

Return On Equity (ROE) as a profitability ratio has no effect on stock returns which means when profitability (ROE) increases, stock returns do not increase and when profitability (ROE) decreases, stock returns do not decrease. This is not in line with signaling theory which reveals that financial information can affect the movement of stock returns which are responded by the market as bad and good signals.

ROE has no effect on stock returns, meaning that high and low ROE will not affect investors in making investment decisions. The results of this study are in line with research (Jefri et al., 2020) which states that ROE does not have a significant effect on stock returns. This proves that ROE cannot be used as an indicator in analyzing stock returns.

3.1 Strategic Measures Analysis

1. Discussion of Profitability

Profitability is one of the indicators of a company's financial performance that investors assess as a factor in measuring the rate of return on investment. Profitability has a good effect on the company's prospects (Kalbuana et al., 2020). Profitability describes the company's ability to make a profit, the greater the level of profit, this indicates the better the company's management. Profitability also reflects the benefits of financial investment (Herdiyana et al., 2020).

In general, investors aim to earn dividend yields generated from the profitability of the company and also earn capital gains from the increasing value of shares by investing in stocks. To maximize revenue, investors can benefit from financial ratios. Financial ratios should also be incorporated into the decision-making process on the basis of determining the right investment strategy. One of the items of financial ratios based on financial statements is the profitability ratio of the company. In other words, the profitability ratio can be a guiding factor for investors in the preference of the stocks they will invest in (Mirgen et al., 2017). The higher the profitability ratio produced by the company, the company can be considered productive in seeking profit or profit. And vice versa, if the lower the profitability ratio produced by the company, then the company can be considered unproductive or inefficient in seeking profits or profits (Taufik & Muliana, 2021).

The profitability ratio used in this study is Return on Equity (ROE). ROE is a tool to measure a company's ability to generate profits using its own capital (Nurhikmawaty et al., 2020). The ability to generate net profit after tax on the capital owned by the company shows better performance. A high ROE reflects the efficiency of the company in using its own capital to generate high profits for the company itself. This ratio indicates management's success in maximizing greater returns for shareholders. The higher the company's ROE, the better its performance, so that more investors will be interested in investing in the company (Komala & Nugroho, 2013).

Return on Equity (ROE) in financial technology companies listed on NASDAQ for the 2013–2021 period consisting of SS&C Technologies (SSNC), Envestnet, Inc (ENV), Green Dot Corporation (GDOT), Equifax Inc (EFX), MarketAxess Holdings Inc (MKTX), and Moody's Corporation (MCO) increased or decreased with an overall average ROE value of 45.08%. The average ROE trend of the six companies shows a downward trend with the lowest ROE recorded in 2017 at -877.285% . This shows that the company is not able to generate profits or profits using its own capital.

2. Discussion of Stock Returns

Stock return is the result obtained from investment. Return can be either a realized return that has already occurred or an expected return that has not yet occurred but that is expected to occur in the future. The calculation of stock return is the difference

between the selling price or current price and the purchase price or the beginning of the period. Thus, it can be concluded that stock returns are reciprocal of investments that have been made by investors or shareholders in the form of profits obtained from buying and selling shares in the capital market.

Investors in buying stocks certainly have the desire to get high returns, but the desire to get high stock returns also has high risk and uncertainty in determining stock returns so it is difficult for investors to predict. Uncertainty in determining stock returns is influenced by very rapid fluctuations in stock prices that can go up and down. The higher the return offered by a security instrument, the higher the risk in the security concerned (high return high risk) (Mangantar et al., 2020).

The return on shares of financial technology companies listed on NASDAQ for the 2013–2021 period consisting of SS&C Technologies (SSNC), Envestnet, Inc (ENV), Green Dot Corporation (GDOT), Equifax Inc (EFX), MarketAxess Holdings Inc (MKTX), and Moody's Corporation (MCO) increased or decreased. The trend of stock returns in 2014, 2015, 2016, 2018, and 2021 was below the overall average stock return of 31.4%. The stock return trend of the six financial technology companies tends to decline with increases that occurred in 2017, 2019, and 2020. This increase was also followed by a decline in stock returns with the largest decline that occurred in 2014 which was 80%.

3. Discussion on the Effect of Profitability on Stock Return

Based on the results of hypothesis testing on the effect of profitability on stock returns, it shows that in the F test, the value of $F_{hitung} < F_{table}$ with F_{hitung} is 0.052655 and the F_{table} value is 2.41, which means that profitability has no effect on stock returns. The significance level of the F test obtained by the variable profitability (ROE) is $0.819406 > 0.05$. This proves that regression is meaningless. Evidenced by the results of the t test which shows the significance value (probability) on the profitability variable (ROE) of $0.8273 > 0.05$ and the t_{hitung} value of $(-0.219265) < t_{table}$ of 1.67469, thus further strengthening that profitability (ROE) has no effect on stock returns. The results of this study are not in line with signaling theory which reveals that financial information can affect the movement of stock returns which are responded by the market as bad and good signals. The financial information in this study is profitability which includes information about Return on Equity (ROE). The results of this study are in accordance with the results of previous research conducted by (Devitra, 2011) on banking companies on the Indonesia Stock Exchange with a panel data regression model that obtained the results that ROE has a negative regression coefficient on stock returns so that it can be said that there is a negative relationship between ROE and stock returns. In this study, it is also known that the regression coefficient value at ROE is -0.004287 , which means that if there is a 1% increase in ROE, the stock return decreases by 0.004%. This shows that profitability (ROE) negatively affects stock returns (Fig. 2).

3.2 Policy Model

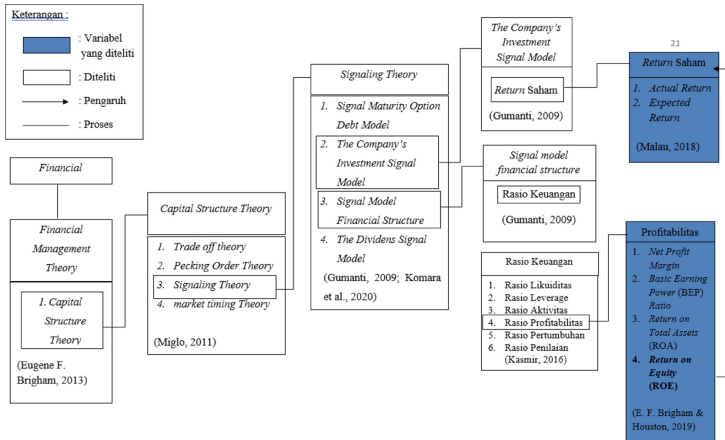


Fig. 2. Policy model for the effect of profitability on stock returns

4 Conclusion

The profitability picture shown by the overall Return on Equity (ROE) shows developments that tend to decline in several periods. The decline occurred in 2015, 2017, 2019, 2020, and 2021, which was caused by a decrease in net profit. This indicates that the rise and fall of the ROE value as an indicator of profitability is influenced by the size of the net profit generated by the company. In this decline, there was a negative ROE value so that it could be concluded that in that year the company could not generate profits through its capital. The picture of stock returns of financial technology companies from 2013 to 2021 shows fluctuating developments tend to decline. The decline in stock returns is reflected in the development of stock price value. If the stock price of the past period (P_{t-1}) is higher than the current stock price (P_t), then there is a capital loss. So it can be concluded that the returns generated by the company are not profitable and considered detrimental. The results of the panel data regression test conducted on the profitability variable on stock returns showed findings that the value of Return on Equity (ROE) as an indicator of profitability had no effect and was not significant.

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