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Effects Of Current Ratio And Debt-To-Equity Ratio On Return On Asset And Return On Equity

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ABSTRACT : *The purpose of a company is to gain profits. The purpose of the present study was to examine the effects of current ratio and debt-to-equity ratio on return on asset and return on equity for companies of the food and noodle sub-sector. A total of 10 companies listed on the Indonesia Stock Exchange (ISX) was sampled from 2014 to 2017. Data were processed using the multiple linear regression analysis with SPSS 24. Results showed that current ratio and debt to equity ratio had a significant effect on return on equity and return on asset. Results of the regression coefficient analysis showed that current ratio and debt-to-equity ratio accounted for 14.9% of ROA, while the remaining 85.1% was explained by other variables, as indicated by the coefficient determinants. The regression coefficient analysis for ROE showed that 61.4% was explained by other variables not studied in this research. Results of the F-test showed a significance value of 0.019 0.05 for ROA and 0.000 0.05 for ROE, meaning that both the current ratio and debt-to-equity ratio had a significant effect on ROA and ROE in food and beverage industry companies listed in Indonesia Stock Exchange.*

Keywords: Current Ratio, Debt-To-Equity Ratio, Return On Assets, Return On Equity

Date of Submission: 20-11-2018 *Date of acceptance: 06-12-2018*

I. INTRODUCTION

Businesses are in fierce competition and growing rapidly. Investors eager to invest their money will take a good financial performance into account. The success or failure of a company in managing finance depends on how their managers manage the companies' finance well. *Financial statements are prepared for internal and external parties for different purposes. For suppliers, it serves to reveal the performance of* the company and the company's ability to pay its debts.

For creditors, it serves to determine the performance of the company in paying the principal and interest thereon. For investors, it serves to ascertain whether the capital they have been invested is either growing or decreased or how it is used.

For potential investors, it provides information in connection with the decision to invest in the company or not. For the government, it serves to determine economic growth, both regionally and nationally, and monitor tax payment (Sumarsan, 2017).

In the preparation of financial statements, there are accounting assumptions and principles, including:

- *One entity, meaning that a company should be a unity and there is a separation between personal property and company property;*
- *Going concern, meaning that an established company should be able to continue its business for an indefinite period of time;*
- *Comparability, meaning that financial statements should be comparable to the financial statements of different periods and to those of other similar companies;*
- *Consistent, meaning that all the accounting methods used to prepare the financial statements should be consistent, so as to give an idea of the earnings to be analyzed.*
- *Timeliness, meaning that the financial statements should be completed timely. Delayed preparation of financial statements cannot add value to its users to make strategic decisions (Sumarsan, 2017).*

According to brealey et al., (2007) the composition of the company's working capital range from 40% of total assets and debts of smooth 25% of total funding company, 60% of the time even owned a financial manager is used to manage current assets. A reason is current assets in short-term investments that quickly turned into another asset type (and Lawrence Gitman, 2009) Based on the results of the above research, current assets need to be managed in disappear play an important role from the overall corporate strategy in order to improve the company's performance (Dong and Su 2010). The company tried to make the right financial decisions with the aim to improve the performance of the company. The problem that arises is the increase in

the company's profit may immolate liquidity aspects of the company. In line with Sigh and Pandey (2008) *current assets investment played an important role in funding decisions mainly concerned with the liquidity aspects of the company. According to Chang et al. (2011) the efficient management of current assets allows companies react quickly to the changes that occur and there is a belief that has an impact on the company's performance.*

The present study selected the food and beverage sub-sector, with the following considerations: (1) in 2017, the food and beverage sub-sector was the largest labor-employing sub-sector, as shown by the table 1:

Table 1. Largest contributor to workforce

Year	Number
2015	3,529,630
2016	4,091,682
2017	3,731,054

Source: Data processed by the authors.

(2) The domestic investment (PMDN) in the food and beverage sub-sector increased by 38.540.
(3) The food and beverage sub-sector had a large growth of non-oil and gas processing industry:

Table 2. Industry Growth

Year	Growth Percentage
2015	7.54%
2016	8.33%
2017	9.23%

Source: Data processed by the authors.

(4) The food and beverage sub-sector had the highest growth in its role with regard to the national GDP.

Table 3. Role with regard to national GDP

Year	Percentage
2015	5.61%
2016	5.97%
2017	6.14%

Source: Data processed by the authors.

(5) The food and beverage sub-sector had the biggest exports, despite the 2016 drop, as shown by the table 4:

Table 4. Largest Exports

Year	US$
2015	US$ 26.45 million
2016	US$ 26.28 million
2017	US$ 31.27 million

Surce: Data processed by the authors.

The present study was a quantitative research, with a sample of 10 companies, 4 years of observation from 2014 to 2017. The companies under study are shown in Table 5:

Table 5. Company Names

Code	Name
ADES	Akasha Wira Internasional
CEKA	Cahaya Kalbar
DLTA	Delta Djakarta
ICBP	Indofood CBP Sukses Makmur
INDF	Indofood Sukses Makmur
MLBI	Multi Bintang Indonesia
MYOR	Mayora Indah
PSDN	Prashida Aneka Niaga
ROTI	Nippon Indosari Corporindo
ULTJ	Ultrajaya Milk Industry

Source: Data processed by the authors.

This study was conducted due to the inconsistent results of previous studies. Borhan et al.[12] (2014) demonstrated that current ratio had a significant positive effect on the financial performance of a company, while debt-to-equity ratio had a negative effect on the financial performance of a company.[13] The present study was supported by Afrifa and Padachi (2016) who showed that liquidity had an effect on ROA and ROE, but leverage had a significant effect on ROE and no significant effect on ROA.[14] Chandra and Sari (2017) demonstrated that the current ratio and debt-to-equity ratio had no significant effect on profitability.

A study by Sari et al.[10] (2018) showed that current ratio had a significant positive effect on return on assets, and so did Saragih, et al. **(2015), Sofie, et al. (2015), Suyono and Gani (2017) and Qurays et al. (2018). On the contrary, Supardi et al. (2016) showed that current ratio had no effect on return on assets, so did Hersandy, et al. (2017), Ambarwati, et al. (2015).**

D'Mello, et al.[22] (2018) showed that shareholders perceive view increasing debt to have a negative impact on their wealth. Suyono and Gani (2017) demonstrated that debt-to-equity ratio had no effect on return on assets.[16] Kumar (2017) indicated that debt-to-equity ratio had no significant effect on stock prices.[17] Similarly, Maskun (2012) showed that current ratio had no effect on stock prices.[18]

Fadilah et al.[15] (2017) showed that debt-to-equity ratio had no effect on profitability, as proxied by return on assets. **Arrad et al. (2018) demonstrated that current ratio had a positive effect on return on equity. Qurays et al.[19] (2017) demonstrated that debt-to-equity ratio had an effect on profitability, as proxied by return on equity.[20] A study by Utami (2016) showed that debt-to-equity ratio had a significant positive effect on return on assets.**

Arguanata and Hidayat (2017) demonstrated that current ratio and debt-to-equity ratio partially had no significant effect on return on assets in a negative direction; **but current ratio, debt-to-equity ratio and total asset turnover had an effect on ROE.**[21] *While Sari and Budiarsih (2014) show that debt-to-equity ratio had no significant effect on Return on Equity.*

II. LITERATURE REVIEW

2.1. Financial statements

Financial statements are reports addressing what happened to assets, profits and dividends, over the last few periods (Brigham and Joel, 2010). Financial statements are the end results of an accounting cycle, which describe the financial condition of a company periodically (Sumarsan, 2017). Financial statements contain the figures of a company's performance and financial condition in the past (historical).

According to Kashmir (2010), the purposes of preparing financial statements are:
(1) to present information on the types and amounts of assets owned by the company at the time;
(2) to inform the types and amounts of liabilities and capital obtained by the company;
(3) to inform the types and amounts of revenue earned in a given period;[20]
(4) to inform the amount and types of expenses incurred by the company in a given period;[9]
(5) to inform the performance of the company's management;
(6) to inform the company's ratio of assets, liabilities and capital;
(7) to inform notes to financial statements.

2.2.[19] *Financial Ratios*

Financial ratios are a technique of analyzing percentages in the financial statements in order to identify, review, and summarize the significant relationships of the company's financial data.[17] *The types of financial ratios are, among others, liquidity ratios, solvency ratio, ability ratios, activity ratios and profitability ratios.*[17]

Liquidity ratios can be the current ratio, quick ratio and cash ratio. This ratio is generally the first attention from financial analysts, because this ratio indicates the company's ability of fulfilling the obligation will be due. Rasio smooth (current ratio) is a comparison between the aktiva well with smooth, smooth debt rasio of the most common measurement is used to determine willingness meet short-term obligation. A low current ratio indicates the occurrence of problems in liquidity. The fluency ratio of companies contrast too high also less good, because it shows the abundance of idle funds that ultimately could reduce profit the company an ideal Ratio prescribed by rule of thumb (General provisions) and consider several factors such as the type of industry and credit habits. Wise investors analyzing the current ratio in more depth by asking questions such as: what is credit available that soon could be taken, whether fixed assets could soon be sold and whether earnings can be expected in the the upcoming. The quick ratio is the ratio between current assets minus inventories with fluency debt. The inventory is current assets liquidity levels are low and often experience fluctuations in price and often result in losses in the event of liquidation. The cash ratio is the ratio between Cash plus short-term securities investments with debt fluency.

Solvency ratio can be the debt ratio and debt-to-total equity ratio (DER). Ability ratio is the interest coverage ratio (ICR). Activity ratios include receivable turnover ratio, inventory turnover and total asset turnover. Debt ratio shows the proportion between the liability which is owned by the entire estate. The higher the precentage, the results tend to be the more robust risk for creditors and investors. This ratio describes the comparison DER, debt and private equity in the funding of the company and shows the ability of private equity firms to meet all obligations. Interest Coverage Ratio (ICR), this ratio is called the closing ratio (Coverage ratio) measures the ability of the fulfillment of the obligation of annual interest with operating profit (EBIT), the extent to which operating profit can be dropped without causing failures in the fulfilment of the obligation to pay interest loans.

Profitability ratios include gross profit margin, operating margin, net margin, earnings per share, dividend payout ratio, return on assets and return on equity.

The present study used current ratio (CRA) and debt-to-equity ratio (DER) as the independent variables. The dependent variables were return on assets (ROA) and return on equity (ROE).

Gross profit margin this ratio measures the efficiency of its production cost control, indicates the company's ability to produce efficiently. In evaluating can be seen the margin per unit of the product, when it is low then the company is sensitive to its competitors. Operating profit margin this ratio measures earnings before interest and taxes Margin against sales net profit ratio measures the net profit after taxes against Income sales per share is the ratio between the net profit after tax by the amount of shares in circulation, if the number is so large indicates that investors increased prosperity dividend payout Ratio, this ratio indicates the magnitude of profit distributed as dividends. Return on Assets. This ratio indicates the company's ability to generate operating profit compared with the total assets invested, the greater the number the ratio indicates that the company is more efficient. Return on Equity his ratio indicates the company's ability to generate net profit after tax compared to the capital itself, the larger the number the ratio indicates that the company is more efficient use of capital itself

Based on the Foundation of theory of research above, the hypothesis of this research is:

H1 = Current Ratio effect significantly to Return On assets
H2 = Debt to Equity Ratio effect significantly to Return On Asset
H3 = Current Ratio effect Return On Equity significantly
H4 = Debt to Equity Ratio effect significantly to Return On Equity

III. METHODS

The present study was a quantitative research using the multiple linear regression analysis. A total of 10 companies was sampled, observed for a period of 4 years from 2010 to 2014. Data were taken from the Indonesia Stock Exchange. This study used the purposive sampling method with the following sample selection criteria:

Number of food and beverage sub-sector companies listed in the ISX	=	*15*
Companies inconsistently issuing annual reports	=	*5*
Number of samples	=	*10*

3.1. Operational Definition of Variables

Dependent Variables

Variables in the research: the research is Return On Assets and Return On Equity.

Return on assets (ROA) measures net income using total assets. It can be formulated as: (Earning Before Taxes: total assets) x 100%

Return on equity (ROE) is a ratio to measure a company's ability to use its resources to generate return on *equity. The formula is: (Earning After Taxes: Total Equity) x 100%*

Independent Variabel

The independent variable in this study is the Current Ratio and Debt to Equity Ratio.

Current Ratio (CRA) measures a company's ability to meet short-term obligations. Can be formulated: (current assets divided Current Liabilities) times 100%. Debt to Equity Ratio (DER) is the ratio between the total debt against the total equity. Can be formulated: (Total Debt divided the amount of equity) times 100%.

3.2. Goodness of Fit Test of the Model

The F-test was used to test the goodness of fit of the research model, aimed at determining whether or not the model was good.

3.3. Classic Assumption Test

A normality test is to test the normality of data. The present study used multicolinearity test and heteroscedasticity test.

3.4. Hypothesis Testing

CRA and DER were tested against the companies' profitability as proxied by return on asset and return on equity using the multiple linear regression analysis, with 5% significance level. The linear equations are:

$ROA = a_1 + b_1\ CRA + b_2\ DER + e$ ..... *(equation 1)*

$ROE = a_2 + b_3\ CRA + b_4\ DER + e$ ..... *(equation 2)*

where: a = Constant
CRA = Current ratio
DER = Debt-to-equity ratio
ROA = Return on assets
ROE = Return on equity
E = Error

3.5. Coefficient of Determination (R^2)

Coefficient of determination (R^2) was used to determine to what extent the model explains the dependent variables. A small value of R^2 indicates the very low ability of independent variables to explain the dependent variables (Ghozali, 2016).

The model of the present study is:

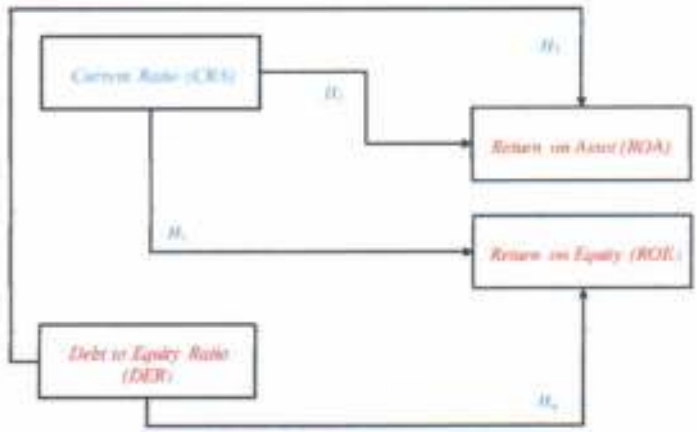

Figure 1 Conceptual Framework

IV. RESULTS

4.1 Model Goodness-of-fit Test (F-test)

Results of the F-test of ROA are shown by the ANOVA table 6:

Table 6. Goodness-of-fit test (F-test) of the model

Model		Sum of Squares	df	Mean Square	F	Sig
1	Regression	0,096	2	0,048	4,423	0,015[b]
	Residual	0,402	37	0,011		
	Total	0,498	39			

[a] Dependent Variable: ROA
[b] Predictors: (Constant), DER, CRA
Source: Authors' data processing

Results of the F-test of ROE are shown in Table 7:

Table 7. Goodness-of-fit test (F-test) of the model

Model		Sum of Squares	df	Mean Square	F	Sig
1	Regression	1,656	2	0,828	13,285	0,000[b]

Residual	2.506	37	0.062
Total	3.962	39	

[a] Dependent Variable: ROE
[b] Predictors: (Constant), DER, CRA
Source: Authors' data processing

3.6. Classic Assumption Test
4.2.1 Data Normality Test

Normality test use Normal P-P Plot Regression shows that data spread around and along the diagonal line, meaning data are normally distributed; thus, the present study satisfies the assumption of normality, for ROA.
For ROE shows that data spread around and along the diagonal line, meaning data are normally distributed; thus, the present study satisfies the assumption of normality.

4.2.2 Multicollinearity Test
Results of the multicollinearity test of ROA are shown in Table 8:

Table 8. Results of regression analysis

	Unstrandardized coefficients			Collinearity statistics	
Model	B	t	Sig	Tol	VIF
1					
(Constant)	−0.063	−0.955	0.346		
CRA	0.033	2.567	0.014	0.529	1.890
DER	0.117	2.854	0.007	0.529	1.890
[a] Dependent Variable: ROA					
Source: Authors' data processing					

Table 8 shows that the Toll value is 0.10 and VIF is 10, indicating no multicollinearity in this study.

Result of the multicollinearity test of ROE are shown in table 9:

Table 9. Results of regression analysis

	Unstrandardized coefficients			Collinearity statistics	
Model	B	t	Sig	Tol	VIF
1					
(Constant)	−0.360	−2.293	0.0280		
CRA	0.069	2.255	0.0300	0.529	1.890
DER	0.484	4.919	0.0000	0.529	1.890

[a] Dependent Variable: ROE
Source: Authors' data processing

Table 9 shows a tolerance value of 0.1 and VIF 10; thus, there is no multicollinearity in the study.

4.2.3 Heteroscedasticity Test

Results of the heteroscedasticity test of ROA are shown that the dots spread randomly above and below zero on the Y-axis and do not show any particular pattern. Therefore, there is no heteroscedasticity in the regression model. Thus, the regression model is good for use to see determine the effects of the independent variables on the dependent variables of the study.

Results of the heteroscedasticity test of ROE are shown that the dots spread randomly above and below zero on the Y-axis. Thus, there is no heteroscedasticity in the study. The regression model can be used to determine the effects of the independent variables on the dependent variable (ROE).

4.3 Hypothesis Testing
As shown in Table 8, the multiple regression equation of independendt variables (CRA and DER) against the dependent variable (ROA) is :
ROA = -0.063 + 0.033 CRA + 0.117 DER + e
From Table 9, the multiple regression equation of independent variables (CRA and DER) against the dependent variable (ROE) is :
ROE = -0.360 + 0.069 CRA + 0.484 DER + e

4.4 Coefficient Determinants

Tabel 10. Model Summary

Model	R	R Square	Adjusted R Square
1	0.439	0.193	0.149

a. Predictors (Constant) : DER, CRA
b. Dependent Variabel : ROA

Source: Author's data processing

As shown in Table 10, adjusted R square of 0.149, meaning that the effects of the independent variable (CRA and DER) on ROA were 14.9 %, while the remaining 85.1 % were affected by other variables not included in the model of the study.

Tabel 11. Model Summary

Model	R	R Square	Adjusted R Square
1	0.646	0.418	0.386

a. Predictors (Constant) : DER, CRA
b. Dependent Variabel : ROE

Source: Author's data processing

While in Table 11, adjusted R square of 0.386 meaning that the effects of the independent variable (CRA and DER) on ROE were 38.6 %, while the remaining 61.4 % were affected by other variables not included in the model of the study.

V. DISCUSSION

5.1 Effects of Current Ratio on Return on Assets

Table 8 shows that CRA has a significance level of 0.014, meaning that CRA has a positive effect on ROA of 0.033, data show that any 1% increase in current assets will cause ROA to increase by 3.3%. Thus, H_1 stating that current ratio has an effect on ROA is accepted.

Results of the present study are consistent with those of previous study conducted by Borhan et al. (2014), indicating that current ratio has a significant effect on financial performance. Afrifa and Padachi (2016) showed that liquidity has an effect on the small- and medium-sized enterprises' profitability as proxied by return on assets.

The present study is in line with that of Saragih, et al. (2015), Sofie, et al. (2015), Suyono and Gani (2017) and Sari et al. (2018), indicating that current ratio has a significant positive effect on return on assets.

5.2 Effects of Debt-to-Equity Ratio on Return on Assets

Table 8 shows that DER has a significance level of 0.007, meaning that DER has a positive effect on ROA of 0.117. Data show that any 1% increase in debt-to-equity ratio will cause ROA to increase by 11.7%. Thus, H_2 stating that debt-to-equity ratio has an effect on ROA is accepted.

The present study is consistent with that of Ardiatmi (2014) which showed that debt-to-equity ratio had a positive effect on profitability. Wibowo and Winarno (2012) showed that debt-to-equity ratio had a negative effect on profitability.

5.3 Effects of Current Ratio on Return on Equity

Table 9 shows that CRA has a significance level of 0.0300, meaning that CRA has a positive effect on ROE of 0.069. Data indicates that any 1% increase in current assets will cause ROE to increase by 6.9%. Thus, H_3 stating that current ratio has an effect on ROE is accepted.

The present study is consistent with that of Borhan et al. (2014) indicating that current ratio has a significant effect on financial performance. In their study of SMEs, Afrifa and Padachi (2016) showed that liquidity had a significant effect on ROE. Similarly, a study by Azad et al. (2018) of registered companies in Pakistan showed that current ratio had a positive effect on return on equity.

5.4 Effects of Debt-to-Equity Ratio on Return on Equity

Table 9 shows that DER has a significance level of 0.0000, meaning that DER has a positive effect on ROE of 0.484. Data show that any 1% increase in debt-to-equity ratio will cause ROE to increase by 48.4%. Thus, H_4 stating that debt-to-equity ratio has an effect on ROE is accepted.
These results are consistent with those of Utami (2016) that showed that debt-to-equity ratio had a significant positive effect on return on equity. Qurays et al. (2018) showed that debt-to-equity ratio had a significant effect on profitability of a company.

VI. CONCLUSION

Table 6 shows that the model fits for accounting for the effects of current ratio and debt-to-equity ratio on ROA, with a significance level of 0.019 0.05.

Table 7 shows that the model also fits for accounting for the effects of current ratio and debt-to-equity ratio on ROE, with a significance level of 0.000 0.05.

The foregoing analysis shows that current ratio and debt-to-equity ratio have a positive effect on ROA at a significance level of 0.019, less than than 0.05. Furthermore, current ratio and debt-to-equity ratio also have a positive effect on ROE at a significance level of 0.000, less than 0.05.

Results of the correlation coefficient test show an adjusted R-squared of 0.149 for ROA. This shows that current ratio and debt-to-equity ratio have a weak effect of only 14.9% on ROA, while the remaining 85.1% are affected by other variables not included in the study, such as cash ratio, account receivable turnover, quick ratio, debt-to-asset ratio, total asset turnover, fixed asset turnover, gross profit margin, net profit margin, and other variables of financial ratios.

Results of the regression coefficient test show an adjusted R-squared 0.386 for ROE. This shows that current ratio and debt-to-equity ratio have a marginally strong effect of only 38.6% on ROE, while the remaining 61.4% are affected by other variables not studied, such as working capital turnover, long-term debt-to-equity ratio, total asset turnover, fixed asset turnover, inventory turnover, net profit margin, and other variables with long-term benefits.

This study has limitations in terms of the period under study and data available on the Indonesia Stock Exchange. Further studies are recommended to include variables related to solvency ratio and activity ratios. Additionally, the macro factors, such as inflation rate, should be included rate in order for more measurability.

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