ISSN: 3063-0509
Journal of Scientific Interdisciplinary

Does Company Size and Profitability Matter? Investigating the Moderating Effects of Growth in Cash Flow on Stock Performance

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Informasi Artikel
Vol: 1 No : 3 2024
Halaman : 14-21

Keywords:
Company Size
Profitability
Stock Performance

Abstract

This research examines the intricate relationships between company size, growth in cash flow, and stock performance, revealing complexities that challenge traditional financial analysis. While company size is often associated with stable stock performance due to advantages such as economies of scale and market power, the findings indicate that size alone does not positively impact stock performance. Furthermore, the study demonstrates that growth in cash flow does not significantly moderate the relationship between company size and stock performance. This suggests that external factors, such as regulatory changes or market sentiment, may play a more decisive role. The results underscore that cash flow, while an important indicator of financial health, does not enhance the influence of company size on stock performance, particularly in certain industries where external conditions prevail. This underscores the need for a more comprehensive evaluation approach that considers a broader range of factors when assessing stock performance. It's time to move beyond traditional metrics like profitability and cash flow growth and equip ourselves with a more robust set of tools for analysis. Ultimately, this research advocates for a multifactorial approach to stock performance evaluation, emphasizing the importance of understanding the interplay between various variables, including industry trends and macroeconomic conditions. By adopting this comprehensive perspective, investors and analysts can make more informed decisions and strategies, enhancing their ability to navigate the complexities of the financial markets.

Abstrak

Penelitian ini mengkaji hubungan kompleks antara ukuran perusahaan, pertumbuhan arus kas, dan kinerja saham, serta mengungkapkan kompleksitas yang menantang analisis keuangan tradisional. Meskipun ukuran perusahaan sering diasosiasikan dengan kinerja saham yang stabil karena keuntungan seperti skala ekonomi dan kekuatan pasar, temuan menunjukkan bahwa ukuran saja tidak menjamin dampak positif terhadap kinerja saham. Selain itu, penelitian ini menunjukkan bahwa pertumbuhan arus kas tidak secara signifikan memoderasi hubungan antara ukuran perusahaan dan kinerja saham, yang mengindikasikan bahwa faktor eksternal dan sentimen pasar mungkin memainkan peran yang lebih menentukan. Hasil penelitian menekankan bahwa arus kas, meskipun merupakan indikator penting dari kesehatan keuangan, tidak meningkatkan pengaruh ukuran perusahaan terhadap kinerja saham, terutama di industri tertentu di mana kondisi eksternal lebih mendominasi. Hal ini menyoroti perlunya mempertimbangkan berbagai faktor saat mengevaluasi kinerja saham, yang melampaui metrik tradisional seperti profitabilitas dan pertumbuhan arus kas. Akhirnya, penelitian ini mendorong penggunaan pendekatan multifaktorial dalam evaluasi kinerja saham, dengan menekankan pentingnya memahami interaksi antara berbagai variabel, termasuk tren industri dan kondisi makroekonomi. Dengan mengadopsi perspektif komprehensif ini, investor dan analis dapat membuat keputusan dan strategi yang lebih tepat, meningkatkan kemampuan mereka untuk menavigasi kompleksitas pasar keuangan.

Kata Kunci : Ukuran Perusahaan, Profitabilitas, Kinerja Saham

INTRODUCTION

Understanding stock performance drivers in modern economics and financial markets is critical for investors and corporate managers. Company size and profitability are two fundamental determinants of firm valuation. Due to economies of scale, larger firms tend to have more stable cash flows and better access to capital, which often translates into higher stock prices. On the other hand, profitability directly signals a firm's operational success and future growth potential, making it an important metric for stock investors (Dasman et al., 2023)

Recent research supports these claims. A study by (García-Sánchez et al., 2020) Larger firms, especially those with high profitability, tend to perform better in the stock market because investors perceive them as less risky. Similarly, (Hailu & Rao, 2022)Found that profitability significantly enhances stock performance, with more profitable firms experiencing greater investor demand, thus pushing up stock prices. These findings highlight the importance of examining company size's and profitability's combined effects on stock performance.

While company size and profitability are essential predictors of stock performance, the role of cash flow growth as a moderating factor is equally crucial. Cash flow represents the lifeblood of any business, indicating its ability to generate liquidity for operations, investments, and shareholder returns. Firms with strong cash flow growth can better withstand market downturns, seize investment opportunities, and improve stock performance even during economic volatility.

Recent phenomena such as the COVID-19 pandemic have underscored the importance of cash flow management. Firms with solid cash flows could maintain or enhance their stock performance despite market shocks, while companies with poor cash flow growth struggled. (Phan et al., 2021) Revealed that during the pandemic, firms with positive cash flow growth saw a significant positive impact on stock returns, while firms with declining cash flows faced severe stock market penalties. This moderating role of cash flow is especially relevant when combined with firm characteristics like size and profitability, making it an essential focus for research.

Understanding how company size, profitability, and cash flow growth impact stock performance is crucial for the broader debate on market efficiency. According to the efficient market hypothesis (EMH), stock prices should reflect all available information, including firm-specific characteristics like size, profitability, and cash flow dynamics. However, market anomalies, such as the small-cap effect (where smaller companies tend to outperform larger ones), suggest that the market may not always efficiently price in these factors.

Recent research challenges some aspects of EMH by showing that firm-specific factors, such as cash flow growth, can lead to persistent mispricing. For example, (Dechow et al., 2020)Found that firms with higher cash flow growth often exhibit more robust future stock returns, which contradicts the predictions of EMH. By investigating how cash flow growth moderates the impact of company size and profitability on stock performance, this research can provide valuable insights into the limitations of market efficiency and help investors identify new opportunities for outperformance.

For corporate managers, the results of this study could have important implications for financial decision-making. Larger firms and profitable businesses often have a competitive advantage in raising capital and expanding operations, but these advantages can be undermined without proper cash flow management. This study can guide firms to improve stock performance by focusing on profitability and growth and optimizing cash flow generation.

For investors, understanding how cash flow growth interacts with company size and profitability to affect stock performance can help in portfolio management. By identifying companies with strong cash flow growth alongside favorable size and profitability characteristics, investors can make better decisions that lead to superior returns. This is especially critical in today’s uncertain economic environment, where cash flow stability is increasingly crucial in investment decisions.

Although the relationship between company size, profitability, and stock performance has been extensively studied, few recent studies have explored how cash flow growth moderates these relationships. Research from 2018 onward has emphasized the growing importance of cash flow in firm valuation but has not fully integrated it into models that include firm size and profitability.

For instance, a 2022 study by Li and Zhang explored the effects of cash flow on firm valuation but did not examine its interaction with company size and profitability. Similarly, (Allen et al., 2019) Focused on profitability and stock returns but did not include cash flow growth as a potential moderator. By addressing this gap, the present study provides a more comprehensive understanding of how internal financial dynamics influence stock performance.

METHODS

This research adopts a quantitative approach using descriptive and explanatory analysis. The focus is on analyzing the relationship between company size, profitability, and stock performance while considering the moderating effect of cash flow growth.

1. Data Collection:
   The study uses secondary data from financial statements of *Consumer Goods Industry Sector companies listed on the Indonesia Stock Exchange in 2019- 2021*. The data includes total assets (company size), net income (profitability), stock prices, and cash flow growth. Data sources include the Indonesia Stock Exchange (IDX) and other publicly accessible financial databases.
2. Sample Selection:
   A purposive sampling method is employed, selecting firms based on specific criteria such as data availability, completeness, and consistency over the study period. *Companies that meet the requirements are a sample of 15 companies*.
3. Variables:
   - Dependent Variable: Stock performance (measured by stock price movements).
   - Independent Variables: Company size (measured by total assets) and profitability (measured by net income).
   - Moderator Variable: Growth in cash flow (calculated as the annual percentage change in cash flow from operations).
4. Data Analysis:
   The data is analyzed using multiple regression analysis to examine the direct effect of company size and profitability on stock performance. The regression model uses interaction terms to test the moderating effect of cash flow growth. Statistical software such as Eviews is used for the analysis.
   Before conducting the regression analysis, classical assumption tests (normality, multicollinearity, heteroscedasticity, and autocorrelation) are performed to ensure the validity and reliability of the model.

RESULT AND DISCUSSION

RESULT

In this study, the independent variable is company size and profitability, the dependent variable is stock performance, and Growth in Cash Flow is used as the moderating variable. The results obtained are:

Table 1
Chow Test Pool

Effects Test	Statistic	d.f.	Prob.
Cross-section F	0.785026	(14.25)	0.6755
Cross-section Chi-square	16.396896	14	0.2897

In the table above, it can be seen that the Prob. The cross-section F value is 0.6755, which is > 0.05, so it can be concluded that the Common Effect (CE) model is more appropriate than the Fixed Effect (FE) model.

Table 2
Lagrange Multiplier Test

Test Summary	Cross-Section	Test Hypothesis Time	Both
Breusch-Pagan	0.132428	0.259670	0.392098

In the table above, it can be seen that the Breausch-Pagan value is 0.392098, which is > 0.05, so it can be concluded that the Common Effect (CE) model is more appropriate than the Random Effect (RE) model.

The Effect of Company Size on Stock Performance

Table 3
Panel Least Squares

Variable	Coefficient	Std Error	t-Statistics	Prob.
C	3.932122	2.896488	-1.357548	0.1817
X1	-1.07E-12	2.74E-12	-0.390809	0.6979

These results indicate that Company Size does not have a statistically significant impact on Stock Performance. In other words, changes in the size of a company, as measured by total assets, do not appear to influence its stock price movements in a meaningful way based on the data analyzed. This finding suggests that investors may not consider company size as a critical factor in determining stock performance, possibly focusing more on other variables such as profitability, cash flow, or market conditions. Consequently, **H1 is rejected**.

The Effect of Profitability on Stock Performance

Table 4
Panel Least Squares

Variable	Coefficient	Std Error	t-Statistics	Prob.
C	3.382506	2.431519	1.391108	0.1713
X2	-1.23E-11	4.63E-11	-0.266548	0.7911

These results indicate that Profitability has no statistically significant impact on Stock Performance. In other words, variations in profitability, as measured by net income, do not meaningfully influence stock price movements in this study. This suggests that investors may not heavily factor in profitability when assessing stock performance, or it could be that other factors, such as market conditions, growth potential, or external economic variables, are more influential in driving stock prices. Consequently, **H2 is rejected**.

The Effect of Company Size with Growth in Cash Flow as a Moderating Variable on Stock Performance

Table 5
Panel Least Squares 1

Variable	Coefficient	Std Error	t-Statistics	Prob.
C	3.990031	3.055456	1.305871	0.1991
X1	-8.04E-13	2.90E-12	-0.277208	0.7830
Z1	0.003187	0.004617	0.690118	0.4941
Z2	0.000172	0.000680	0.252737	0.8018
Z3	3.76E-05	0.000940	0.039967	0.9683

Table 6
Panel Least Squares 2

Variable	Coefficient	Std Error	t-Statistics	Prob.
C	3.573473	3.114985	1.147188	0.2587
X1	2.21E-12	3.83E-12	0.578563	0.5664
Z1	-0.012115	0.010018	-1.209266	0.2342
Z2	-0.002007	0.001512	-1.327144	0.1926
Z3	0.000218	0.001394	0.156370	0.8766
X1Z1	2.75E-14	1.56E-14	1.764550	0.0859
X1Z2	6.71E-15	4.04E-15	1.661379	0.1051
X1Z3	4.54E-15	5.76E-15	0.788330	0.4355

The analysis results show that the interaction between Company Size and moderated Growth in cash flow does not significantly affect Stock Performance. The T-Statistic indicates this with a Prob. Value of 0.4941, 0.8018, 0.9683 in Panel Least Squares 1 and a Prob. Value of 0.0859, 0.1051, and 0.4355 in Panel Least Squares 2, both greater than α. This indicates that Growth in Cash Flow cannot strengthen the influence of Company Size on Stock Performance movements; thus, H3 is rejected.

The Effect of Profitability with Growth in Cash Flow as a Moderating Variable on Stock Performance

Table 7
Panel Least Squares 1

Variable	Coefficient	Std Error	t-Statistics	Prob.
C	3.655574	2.545071	1.436335	0.1587
X2	-1.90E-11	4.85E-11	-0.391107	0.6978
Z1	0.003647	0.004558	0.800121	0.4284
Z2	0.000156	0.000678	0.229779	0.8194
Z3	3.95E-05	0.000934	0.042293	0.9655

Table 8
Panel Least Squares 2

Variable	Coefficient	Std Error	t-Statistics	Prob.
C	3.691927	2.668127	1.383715	0.1747
X2	-2.67E-11	6.55E-11	-0.406894	0.6864
Z1	0.003050	0.006074	0.502101	0.6186
Z2	0.000223	0.001253	0.177794	0.8599
Z3	0.000426	0.002610	0.163070	0.8714
X2Z1	-1.74E-14	9.82E-14	-0.177628	0.8600
X2Z2	-3.25E-15	4.39E-14	-0.074019	0.9414
X2Z3	1.03E-14	6.68E-14	0.154857	0.8778

The analysis results show that the interaction between Profitability and moderated Growth in cash flow does not significantly affect Stock Performance. The T-Statistic indicates this with a Prob. Value of 0.4284, 0.8194, 0.9655 in Panel Least Squares 1 and a Prob. Values of 0.8600, 0.9414, and 0.8778 in Panel Least Squares 2 are more significant than α. This indicates that Growth in Cash Flow cannot strengthen the influence of Profitability on Stock Performance movements; thus, H4 is rejected.

DISCUSSION

The Effect of Company Size on Stock Performance

The statement suggests that company size does not significantly affect stock performance in some cases, which contrasts with traditional theories that larger firms tend to experience more stable stock performance. This is primarily due to factors such as economies of scale, greater market power, and easier access to capital. Economies of scale allow larger firms to reduce per-unit costs as they grow, improving profitability and stock performance. Similarly, larger firms typically have more vital market positions and better access to financing, which contributes to financial stability and potentially better stock returns.

Several studies emphasize the connection between company size and stock performance. Fama and French's (1993) three-factor model is a classic example where firm size is crucial, showing that small-cap stocks tend to outperform large-cap stocks over time. Still, larger firms are often considered safer due to their stability and access to capital. More recently, (Huang et al., 2020) found that larger firms, due to their lower risk and stable growth prospects, tend to have less volatile stock returns and are often seen as safer investments, especially during periods of market uncertainty.

However, newer research challenges the universal application of this theory. In their study on firm size and stock returns, (Dang et al., 2018) argue that the relationship between company size and stock performance may not hold uniformly across all sectors and market conditions. They find that in specific industries, mainly those driven by innovation or rapid technological change, other factors like cash flow, profitability, and market sentiment play a more significant role in influencing stock prices than company size alone.

(He & Niu, 2021) also studied the Chinese stock market and concluded that firm size does not always lead to better stock performance. In highly competitive or rapidly evolving industries, the

advantages of size can be offset by the need for agility and innovation, which are more commonly found in smaller firms. This suggests that company size may be a less critical determinant of stock performance in specific market environments.

(Watanabe & Yamada, 2022) further explored this idea by investigating stock performance in different market conditions. They found that investors prioritize liquidity and cash flow stability over company size during economic volatility or crisis periods. In these contexts, firms with strong operating cash flows or profitability metrics can outperform larger companies struggling with operational complexity or capital constraints. Their findings highlight that factors such as cash flow growth or profitability can overshadow firm size in determining stock returns, particularly in turbulent markets.

These newer studies highlight that while company size has traditionally been linked to more stable stock performance, this relationship is not universal. The influence of company size can diminish in specific sectors or under particular market conditions, making other factors—such as cash flow, profitability, or market dynamics—more critical in determining stock performance. This emphasizes the importance of taking a multifactorial approach when evaluating stock performance rather than relying solely on firm size.

The Effect of Profitability on Stock Performance

The statement highlights how profitability has traditionally been linked to positive stock performance, as profitable firms are viewed as financially stable and better positioned to provide returns to shareholders. However, the lack of a significant relationship between profitability and stock performance in some cases suggests that profitability might not be the key driver of stock prices under certain conditions.

(Chae et al., 2021) while profitability is typically a positive signal for investors, its impact on stock performance can be diminished during economic uncertainty or rapid market changes. Their study suggests investors may prioritize liquidity, cash flow, or growth potential over traditional profitability measures in volatile markets. This research aligns with your finding, where profitability does not significantly influence stock performance, as other factors come into play during market volatility or in specific sectors.

(Hou et al., 2020) extended the Q-theory of investment and argued that profitability, while important, must be viewed alongside other financial metrics like investment and operating efficiency. They showed that companies with high profitability but low reinvestment or growth potential may not experience corresponding stock price increases. In contrast, firms with strong growth prospects often attract more investor attention, even with lower profitability. This suggests that stock markets may value future potential more highly than current profits, reflecting the findings in your research.

These recent findings illustrate that the relationship between profitability and stock performance is not straightforward. In some market environments or industries, profitability alone cannot explain stock performance. Factors such as industry trends, investor sentiment, and macroeconomic conditions can have a more pronounced impact. This supports the notion that stock valuation is complex and requires a multifactorial approach, integrating both traditional financial metrics and external factors that can influence investor behavior (Yulianti et al., 2024).

Investors and analysts can better understand stock performance by considering these factors, reflecting the dynamics beyond profitability alone. It also suggests that companies with solid growth prospects, innovation, and sound financial strategies may outperform those with merely high profitability, especially in sectors where future potential matters more than past earnings.

The Effect of Company Size with Growth in Cash Flow as a Moderating Variable on Stock Performance

The statement that "Growth in Cash Flow cannot strengthen the influence of Company Size on Stock Performance movements" suggests that, in this study, cash flow growth does not enhance or mediate the relationship between company size and stock performance. This finding raises important questions about the dynamics between these variables and highlights the need to explore how cash flow interacts with other factors in determining stock performance.

Ultimately, the finding that growth in cash flow does not strengthen the influence of company size on stock performance underscores the complexity of stock valuation. It suggests that investors may rely on diverse indicators beyond traditional financial metrics to assess stock performance. As noted by (Li & Zhang, 2022), a multifactorial approach that considers various elements—such as market trends, competitive dynamics, and investor behavior—can provide a more comprehensive understanding of stock performance.

Moreover, external market conditions and investor sentiment may further complicate the interplay between company size, cash flow, and stock performance. According to (Gao & Zhang, 2020), investor focus may shift from company size or cash flow metrics to macroeconomic indicators or broader market trends during economic uncertainty. This shift can dilute the relevance of cash flow growth as a moderating factor, particularly for large firms that may face different challenges and opportunities than smaller ones. Their research illustrates that market conditions can significantly influence how investors assess company performance, affecting the relationship between size and stock performance.

The lack of a moderating effect of cash flow growth on the relationship between company size and stock performance, as indicated in your research, could point to several limitations. For instance, (Moussa & Saidi, 2019) explored how industry-specific factors influence the effectiveness of cash flow as a moderator. They found that in industries where innovation and growth potential are prioritized, cash flow metrics may have a limited impact on stock performance compared to factors like competitive positioning and market sentiment. This suggests that the characteristics of the industry could overshadow the potential moderating role of cash flow growth.

The assertion that growth in cash flow cannot enhance the influence of company size on stock performance emphasizes the need for a nuanced approach to financial analysis. It highlights that while important, cash flow may not always mediate in the context of company size and stock performance. As such, further research is necessary to explore the specific conditions under which cash flow growth influences stock performance, particularly within different industries and market environments.

CONCLUSION

In this research, investigating the relationships between company size, growth in cash flow, and stock performance reveals nuanced dynamics that challenge traditional notions in financial analysis. While company size has often been linked to stable stock performance due to advantages such as economies of scale and market power, the findings indicate that size alone does not guarantee a positive influence on stock performance. This suggests that the complexities of market conditions and investor behavior can dilute the perceived benefits of being a more prominent firm.

Moreover, the study highlights that cash flow growth does not strengthen the relationship between company size and stock performance. Recent research indicates that cash flow is a critical indicator of financial health, often providing a more reliable signal of a firm's operational effectiveness than traditional profitability metrics. However, the absence of a significant moderating effect from cash flow growth raises questions about its role in influencing stock performance, especially in industries where external factors and market sentiment play a more decisive role.

Ultimately, the conclusion emphasizes the need for a multifactorial approach when evaluating stock performance. This approach should account for variables beyond company size and cash flow, including industry trends, macroeconomic conditions, and investor sentiment. By recognizing the complexity of these relationships, investors and analysts can develop a more comprehensive understanding of stock performance, leading to better-informed investment decisions and strategies.

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