

## Stock Market Reaction to the Event of Indonesia's General Election Events in 2019

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**ABSTRACT :** An event must have information that can affect the stock market. One of the events allegedly having information for the capital market is the election which is part of political events. This study aims to look at the stock market reaction to information in the events of the Indonesian elections in 2019 by looking at the presence or absence of abnormal returns. This study uses the event study method with a sample of 44 companies listed on the LQ45 index on the Indonesia Stock Exchange. The results of this study found a significant abnormal return on elections and election announcements, this indicates that the election events contain important information that causes the stock market to react.

**KEYWORDS :** *Event Studies, Market Reaction, Abnormal Return, Stock Market, Election*

### I. INTRODUCTION

Economic development which is assisted by the development of technology and information nowadays has given rise to various choices for the community in spending or investing their capital. One of the choices pursued by the public is investing in the capital market. In the capital market there are two basic financial management decisions consisting of investment decisions and funding decisions. Funding decisions will be made by companies by determining financial instruments to be traded such as stocks, bonds, warrants, rights, mutual funds, and various derivative instruments such as options, futures, and others to get capital from the public while investment decisions will be made by investors through several stages to make an investment and this study will focus on stock. Investment decisions will be made by investors through several stages to make an investment. Stages in the investment decision include determining the investment objectives, determining the policy of an investment, determining the best strategy in selecting portfolios, determining the best assets, and measuring and evaluating portfolio performance (Tandelilin, 2010:12). Investment itself is an investor's trust in investing a number of funds made at this time with the aim of obtaining profits in the future. Investors will be in a situation of uncertainty between the return to be received and the risk that will be faced. The great risk faced will result in a large return of expectations as well <sup>2</sup>. One of the guidelines that can be used by investors to get a picture of risk and return expectations is information.

Fama (1970) in his concept of Efficient Market Hypothesis (EMH) states that new and relevant information that is available or published to the public, if it can be fully described in the prices on the market, then the market can be said to be an semi strong form market efficiency. Economic events that can affect the stock market are inflation, changes in currency exchange rates, fiscal policy, monetary policy, interest rates, dividend policy, corporate strategy and the decision of the General Meeting of Shareholders (GMS) while non-economic events that can affect the stock market are the environment, human rights issues, terrorist acts, demonstrations, and political events that are very sensitive to market conditions <sup>4</sup>. One study that involves an analysis of price behavior around the time of an announcement or event that contains information is called an event study <sup>5</sup>. The content of information in an event is marked by the presence of abnormal return.

There are many event study studies conducted abroad related to the impact of political events on the stock market. Khan, Rehman, & Hussain (2016) found the impact of political events on the stock markets in Pakistan. Similar research was also found by Sai (2018) in his research in India, Chen, Feng-Shun, & Chun-Da (2005) in Taiwan and Ahmed (2017) in Egypt. One political event that has a large impact on the stock market is elections. Elections are one of the political events that have a macro effect. Although the election is a non- economic event, the election still has a big influence in maintaining the stability of the country<sup>10</sup>. The election process is a means of determining the direction of regulation of a country, a good quality regulation will later give a positive impact on a country's capital market going forward<sup>11</sup>. Election abroad can determine the country's ideology in certain periods that can influence investors' decisions in investing their capital in the stock market<sup>12</sup>.

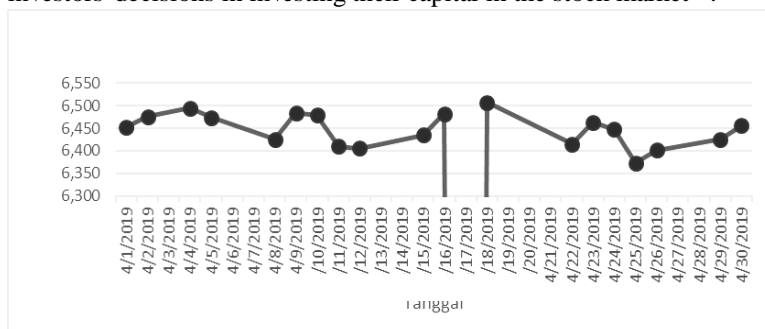


Figure 1. IHSIG values in 2019 election month. Source: Secondary Data, Yahoo Finance, 2019

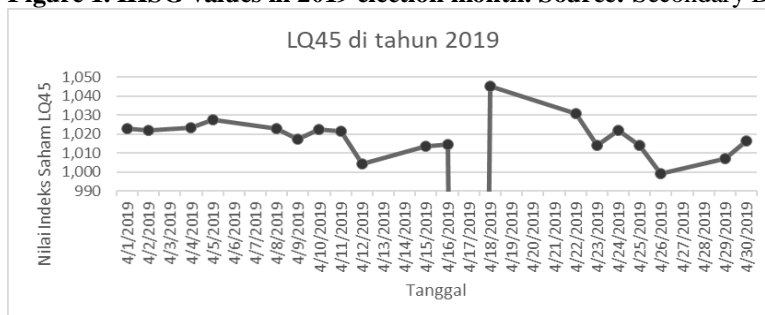


Figure 2. LQ45 values in 2019 election month. Source: Secondary Data, Yahoo Finance, 2019

In Indonesia the Composite Stock Price Index (IHSIG) showed an increase a few days before the 2019 general election from the value of 6,406.86 points before the election to 6,507.22 points after the election. LQ45 which is an index of measuring the price performance of 45 stocks that have high liquidity and is supported by good company fundamentals also shows the same increase symptoms. This increase shows the market is still open opportunities for investors to conduct investment activities, investors want an increase in return as payment for uncertainty in the capital market when the election events occur<sup>13</sup>.

Several studies have been conducted to determine the effect of elections on the capital market, Gobran & Bacon (2017) found the effect of election victory in America on the stock market. Hung (2013) even found that the election in America had a sensitive influence on the capital market in Taiwan, in the country of Indonesia, Permata Sari, Ayu Purnamawati, & Herawati (2017) found that the activities of the American presidential election had no effect on the Indonesian capital market. Indonesia election in 2014 were found to have an impact on the capital market which was marked by positive abnormal returns, this study was conducted by Diniar & Kiryanto (2016) while Mekel & Sihotang (2015) found a result that there were no abnormal returns before and after the presidential election in Indonesia in 2014 on shares of construction companies, infrastructure and utilities. The legislative election events also did not have a significant impact on differences in abnormal returns before and after the election took place<sup>2</sup>.

The inconsistencies in the results of previous studies and because in 2019 Indonesia held the executive and legislative elections for the first time simultaneously made researchers interested in conducting a similar study under the title "Stock Market Reaction to The Event of Indonesia's General Election Events in 2019". Here is a hypothesis formed based on efficient market theory and previous studies

H1: There was a reaction on the stock market with the existence of abnormal returns in the event period during the 2019 general election in Indonesia.

H2: There was a reaction on the stock market with the existence of abnormal returns in the event period during the announcement of the 2019 general election in Indonesia.

Researchers are also interested to know whether there is a difference that occurs on the day the election takes place and the day of the election announcement. The different reactions show the discrepancy between investors' expectations and the election winner. In 2019 after Election Day, the official institution of the General Election Commission provides a real vote counting website that is updated regularly for the vote count until the day the election announcement is announced. In this condition, investors should be able to predict or expect the results of the general election appropriately. Thus, the next hypothesis is as follows.

H3: There was a difference in reaction in the event period during the 2019 general election with the announcement of the 2019 general election in Indonesia.

## II. LITERATURE REVIEW

### 1. Efficient Market Theory

In general an efficient market is a market that reflects its stock price based on the basic information available and related to the company<sup>19</sup>. Fama (1970) presents three main forms of market efficiency based on the three types of information. The three types of forms are: (1) weak forms where the prices of securities fully reflect past information, that are tested with a test for return predictability, (2) semi-strong forms where securities prices fully reflect all published information, that are tested with event studies and (3) strong forms where securities prices fully reflect all available information including private information, that are tested with a private information test.

### 2. Event Study

According to Oktavia (2015) event study is a study that describes a research technique to see the impact of a particular event on changing dimensions or variables. Event studies can be used to test the information content of an event<sup>21</sup>. Event studies are conducted to observe the movement of stock prices in the capital market when an event occurs whether there is an abnormal return on investment due to the event. Fama et al, (1969) in<sup>22</sup> states that if an event contains information for the market there should be a nonzero stock-price reaction that is marked by abnormal returns.

### 3. Abnormal Return

Abnormal return is the difference between the stock's actual return and its expected return (Tandelilin, 2010:240). Market reaction can be measured using abnormal returns. Abnormal return values can be positive and negative values. If the abnormal return is positive mean the actual return is greater than the return expected, this indicates that investors believe in investing their funds. If the abnormal return is negative the actual return is lower than the expected return by the investor, this indicates that investors do not believe in investing their funds. Several calculation models are used to calculate abnormal returns (Hartono, 2017:667) such as mean-adjusted model, market model and market-adjusted model.

## III. RESEARCH METHOD

This research uses event study method to find out the market reaction during the election events in Indonesia in 2019. The location of this research was conducted at the Indonesia Stock Exchange (IDX) which can be accessed at [www.idx.co.id](http://www.idx.co.id) and the yahoo finance website. The data used is the daily closing price of shares in November 2018 to April 2019 for companies listed in the LQ45 index. This research takes election date on 17 April 2019 and election announcement on 21 May 2019 where this date will be used as t0. The event period used in this study was 11 days, which consisted of 5 days before the event and 5 days after the event. Because this research uses the market model, there must be an estimation period, where this study uses 100 days from t-5 to t- 105 for the estimated period. There are steps that must be taken to test abnormal returns in an event such as calculating the daily actual return of shares, expected returns, abnormal returns, standardized abnormal returns.

The formula for calculating the actual return is as follows:

$$R_{it} = \frac{P_t - P_{t-1}}{P_{t-1}}$$

Definition:

$R_{it}$  = Individual Return of Stock i at Time t.

$P_t$  = Closing Price of Stock i at Time t.

$P_{t-1}$  = Closing Price of Stock i at Time t-1.

The formula for calculating the expected return using Ordinary Least Square regression is as follows:

$$R_{it} = \alpha_i + \beta_i * R_{Mt} + \epsilon_{i,t}$$

Definition:

$R_{it}$  = Return Realization of i-Securities in The t-Estimation Period.

$\alpha_i$  = Intercept for i-Securities.

$\beta_i$  = Slope Coefficient which is The Beta of The i Amount of Securities.

$R_{Mt}$  = Return of The Market Index

$\epsilon_{i,t}$  = Error of Residual i-Securities in The t-Estimation Period.

The formula for calculating the abnormal return is as follows:

$$RTN_{i,t} = R_{i,t} - E[R_{i,t}]$$

Definition:

$RTN_{i,t}$  = Abnormal Return of i-Securities in The t-Event Period.

$R_{i,t}$  = Actual Return that Occurs for The I-Securities in the t-Period.

$E[R_{i,t}]$  = Expected Return of i-Securities for The t-Event Period.

The formula for calculating the standardized abnormal returns is as follows:

$$RTNS_{i,t} = \frac{RTN_{i,t}}{KSE_i}$$

Definition:

$RTNS_{i,t}$  = Abnormal Return Standardization of Securities i on The t-Day in The Event Period

$RTN_{i,t}$  = Abnormal Return of Securities i on The t-Day in The Event Period.

$KSE_i$  = Standard Error of Estimation for i-Securities.

The data analysis tool used to test the first and second hypotheses is the t-test table by comparing the portfolio standardized abnormal return with the values in the t-table. The third hypothesis will be tested using paired sample t-test data analysis.

## IV. RESULT AND DISCUSSION

### 1. Abnormal Return Test

Abnormal return testing is done by comparing the standardization of abnormal returns with the values in table t. Abnormal return testing is done by comparing the standardization of abnormal returns with the values in table t. If the standardization of abnormal return on t day has a higher value than table t which has a value of 1.684, it means that there is a significant abnormal return on that day.

**Table 1.** Average Abnormal Return (AAR) & Average standardized abnormal returns (ASAR)

Window Period	Presiden Election			Presiden Election Announcement		
	AAR	ASAR	Note	AAR	ASAR	Note
-5	-0.0047	5.845	Significant*	-0.0045	6.735	Significant*
-4	-0.0057	7.217	Significant*	-0.0221	29.72	Significant*
-3	-0.0014	0.936	Not Significant	-0.0186	25.09	Significant*
-2	0.0028	4.793	Significant*	-0.0030	10.97	Significant*
-1	0.0086	9.928	Significant*	0.0201	31.29	Significant*
0	0.0000	0.000	Not Significant*	0.0155	20.91	Significant*
1	0.0009	5.228	Significant*	0.0004	5.27	Significant*
2	-0.0106	13.613	Significant*	0.0186	26.3	Significant*

3	0.0160	14.559	Significant*	0.0067	10.12	Significant*
4	-0.0006	1.442	Not Significant*	0.0131	16.07	Significant*
5	-0.0141	15.313	Significant*	-0.0043	10.39	Significant*

Notes: \* $p > 1.684$ .

Based on table 1, test results show the existence of abnormal return in the event period during the 2019 elections in Indonesia. Significant abnormal returns are found in t-2 (0.003), t-1 (0.009), t + 1 (0.001), t + 2 (- 0.011), t + 3 (0.016) which indicate that the election event has information that makes the market react. There is no abnormal return on t (0) due to the closing of the rice market on general election day, however, we can see the market reacting on the day after the general election, namely at t + 1, t + 2 and t + 3. This result is supported by several studies which also found the existence of abnormal returns in the electoral event period as in the research of Pamungkas et al, (2015), Oktavia (2015) also Santoso & Sri Artini (2015). For the 2019 election announcement there is also a significant abnormal return on all days during the event period, this means that the election announcement event also has information that also makes the market react. This result is supported by several studies which also found the existence of abnormal returns in the period of the election events, namely in the research of Purnama et al, (2015) and Wahyuni et al, (2017)

## 2. Paired Sample T Test

Here we try to find out whether there are significant differences in abnormal returns during elections and at the announcement of elections.

**Table 2.** Paired Sample T-Test Test Results

Variable	Amount	T-Value	Sig (2-Tailed)	Criteria	Description
AAR of Election – Election Announcement	11	-0,662	0,523	0,05	Not significant

Based on table 2, abnormal return in the event period during the election and announcement of the 2019 election shows a t value of -0.662 and a significance value of 0.523. Significance values above 0.05 indicate there is no difference in abnormal returns in the event period during the general election and the announcement of the 2019 general election in Indonesia. These results illustrate that the results of the 2019 election announcement are in accordance with predictions from market participants and it can be said the market can handle this information well so that the reaction that occurs in the announcement of the election is not much different from election day.

## 3. Description of Research Result

To find out the type of reaction experienced in the market, a descriptive analysis of each sample grouping was performed.

**Table 3.** Descriptive Statistics Analysis Results

Samples	Minimum	Maximum	Mean	Std. Deviation
General Election	-0.014000	0.016000	-0.000818	0.008483
General Election Announcement	-0.022000	0.020000	0.002091	0.014398

Based on table 2, average abnormal return (AAR) value during the election event period shows an average of -0,000818 with a standard deviation (SD) of 0.008483. This value has a negative value and this means that the election event has negative information for the market which is characterized by a negative tendency by investors in purchasing company shares. The lowest AAR value is -0.014000 at t + 5 (five days after the election) and the highest AAR value is 0.016000 at t + 3 (three days after the election).

The Average Abnormal Return (AAR) value during the election announcement period shows an average of 0.002091 with a standard deviation (SD) of 0.014398. This value has a positive value, this means that the election announcement event contains positive information content for the market which is marked by a positive tendency by investors in purchasing company shares. The lowest AAR value is -0.022000 on t-4 (four days before the election announcement) and the highest AAR value is 0.020000 on t-1 (one day before the election announcement).

## V. CONCLUSION

The conclusion of this research is the 2019 election events in Indonesia caused a reaction for the stock markets represented by companies listed on the LQ45 index. Elections and election announcements do not have a statistically significant difference, but there are differences in the characteristics of each event that occurs. The reaction that occurred in the 2019 election event was negative which indicated investor mistrust in investing their capital in the Indonesian stock market while the reaction that occurred in the announcement of the election was positive which signaled the trust of investors in investing capital owned in the Indonesian stock market. From the results of this study investors must realize that it is not only economic events that can affect the capital market but non-economic events, especially political events, also have an impact on the capital market. Investors must be able to manage all the information that is around them to measure the risk and return of expectations that they will face carefully and carefully. Future studies can re-examine using the same variables in this study with different years to strengthen this study. Future researchers can also conduct similar studies using indexes based on each sector.

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