

# Stock Market Reaction to the 2014 Indonesian Presidential Election

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**Background:** A Presidential Election is one of the political events which influences the stock market. There are different occurrences of the stock market reactions in some countries, which led to uncertain conditions of the stock market around the time of the presidential election event. **Purpose:** This study aims to investigate whether there is market reaction, represented by abnormal average return (AAR), cumulative abnormal return (CAR), and average abnormal trading volume (AATV), around the 2014 Indonesian presidential election based on Efficient Market Hypothesis. **Method:** The type of this study is a quantitative approach which uses market data such as stock prices and trading data, with measurable data and statistical analysis to test the hypothesis. This study uses an event study method with 11 days of event period on companies listed in Kompas-100 index as sample. One-sample Kolmogorov-Smirnov test was used to test the data distribution. Then, significance testing is done, to test the hypothesis by using one-sample t-test, paired t-test or Wilcoxon signed-rank test. One-sample t-test is used to test each group H1, H2, H3, H4, H5, and H6. **Result:** This study acknowledges that the market is semi-strong efficient indicated by a quick price adjustment around candidate and result announcements. In accordance with AAR, the AATV can also be seen from D+2 until D+5 of the result announcement. **Conclusion:** AAR shows a significant difference starting from before the official candidate announcement. Meanwhile there are no different CAR and AATV around the candidate and result announcements.

**Key words:** *AATV, abnormal return, Efficient Market Hypothesis, event study, market model.*

## Introduction

A close relationship between political and economic conditions is well known (Prihandono, 2012; Setianto and Manap, 2011). For example, several good (bad) political announcements

could generate positive (negative) abnormal return in the Nepal stock market (Dangol, 2008). A Presidential election is one of the examples of political events. Based on researches in several countries, stock markets are influenced by elections. In America, the stock market often hits major bottoms about two years before presidential elections and rises through the end of election years (Nickles, 2004). Nickles explained that this was because the executive branch of government is influencing fiscal policy and past administrations have often used fiscal policy in a manner designed to pump up the economy just prior to a presidential election. These pre-election actions and campaign promises have often created euphoria among voters and investors (Harymawan et al., 2017), because economic stability followed by political stability will provide the feeling of safety among investors to invest their fund, and the investors' expectation of the new president is reflected in the change of price and volume of stock trading in the stock market.

This phenomenon relates with the fundamental theory of market efficiency. In an efficient market, all available information will be embodied in the stock price, implying that investors cannot earn abnormal returns. Efficient market theory is proven by what already happened in several countries, not only in America, but also in Taiwan, South Korea, Philippines, including Indonesia that had an abnormal positive return in the pre-election period (Pabyantara and Dharmaputra, 2019). However, the same research revealed that the presidential election in Singapore didn't have a significant effect on the stock market because the ruling party in Singapore controlled the process of election, so the result of the presidential election in Singapore was predictable. Based on Uncertain Information Hypothesis, the positive abnormal return in pre-election period relates to uncertainty during that period and it is also affected by the level of politics, economy, press freedom, and the outcome of the election (Liu, 2007). Another research shows that when the outcome of the election brings about a change in the political orientation of the government, it will increase the uncertainty, and the market tends to react in a more volatile manner (Bialkowski et al., 2006).

Research conducted by Liu during the Indonesian presidential election in 2004 had a different result from the one conducted by Trisnawati. It found that there was no significant difference in the average abnormal return and average trading volume activity on LQ-45 before and after the presidential election in 2004. However there are different AARs before and after the presidential election in 2009. Based on their analysis, no differences in AAR and ATVA showed that investors tend to wait and see in the presidential election period and spend their fund on short term investments (Trisnawati, 2014).

This study uses the Kompas-100 index, different from previous research that used LQ-45 as the sample, because it is considered to reflect stock market values due to the value of market capitalisation around 70% from IHSG and the movement correlation was more than 95% (Vilawati, 2012). Another difference is the previous researches focused on the date around the

date of the election, however this study focuses on two important dates in the presidential elections: when there is new information such as KPU (General Election Commission) announcement of the candidates, and the winner of the presidential election in 2014.

So that is the reason why this study analyses the return and trading volume around those dates to see whether there is a market reaction or not in Kompas-100. It also compares the market reaction between around the date of the candidate announcement and the result announcement. If there is an immediate market reaction, it means that the market is a semi-strong efficient market. This result of this study shows that there will be significant differences compared to the previous election. The result of this research can also be an additional reference and comparison for future researches about efficient market hypotheses in the Indonesian stock market.

This study is structured as follows: Section 1 explores the background of this research. Section 2 explains about theory and research hypothesis development. Section 3 explains the research methodology. Section 4 explains the result. Section 5 discusses the obtained result. Section 6 concludes the research result.

## **Literature Review**

### ***Signalling Theory***

In explaining the signal theory, Jogiyanto argues that the published information will give a signal to investors in considering their investment decision. If the event contains positive information, the market is expected to react when the information is received by the market (Sihotang and Mekel, 2015).

### ***Efficient Market Hypothesis***

Efficient market is defined by Jones as the condition when the prices of securities quickly and fully reflect all available information consisting of past, current, and reasonably inferable information about the assets, because in efficient market condition, investors will assimilate relevant information into prices in making their buy-and-sell decision. Fully reflect means the market puts a valuation on securities that is unbiased by using all available information so the market does not systematically misinterpret the value implication of information about stock (Scott, 2012).

There are three basic forms of market efficiencies such as: (1) weak form: historical price and volume data should already be reflected in current prices and should be of no value in predicting future price changes. (2) semi-strong form: the market can quickly incorporate all such

information into prices, so that the current price reflects all available information. (3) strong form: the prices of securities fully reflect all information, public and non-public, so no investors should earn, over a reasonable period of time, abnormal rates of return by using that information because this information is reflected in the prices of securities (Jones, 2001).

On the other side, Jogiyanto (2012) classified efficient market not only from the information point of view named “informationally efficient market”, but also from the way that the investors make decision by considering the available information called “decisionally efficient market”. The difference is that in the decisionally efficient market, availability of information cannot guarantee that the market will be efficient.

### ***Event Studies***

An event study is a study to learn about the market reaction to an event in which the information is being published (Jogiyanto, 2012). It can also be used to test the information content by seeing the market reaction from the price of securities indicated by the abnormal return. If the information content is there, abnormal return will exist. In order to test the market efficiency in a semi-strong market from information, we can analyse it from the abnormal return and how fast the reaction is.

Meanwhile to test the efficiency of the decision, these things are considered: (1) abnormal return or any remaining portion of the actual return after adjusting for company’s return, (2) how fast the reaction or the speed of price adjustment, (3) economic value or how investors differentiate whether the information or announcement contains economic value or not, (4) accuracy of reaction or how investors analyse the information to make sure their decision is not fooled by the market.

There are several empirical results of event studies: (1) stock split; although stock split has no economic value, stock split is considered as a good sign of the prospect of the company, thus, the reaction will be positive, (2) initial public offering (IPO): given the risk the underwriter faces trying to sell a new issue when the true price is unknown, the stock is under-priced to ensure its rapid sale. Then the investors buying the initial offering may be able to earn abnormal return (Jones, 2001). (3) accounting information: market value from the company shows the present value and cash flow (Jogiyanto, 2012). Investors will see the accounting information about their cash flow and net income as the signal showing the value of the firm.

### ***Average Abnormal Return around the Candidate Announcement***

Four out of five countries showed abnormal returns during their pre-election period due to the existence of uncertainty in those four countries (Liu, 2007). There was an uncertain condition in the 2014 presidential election especially around the announcement of the candidate because

the voters and investors still had several speculations about the winner and the next economic programs. Therefore, there should be an abnormal return around the candidate announcement. While for the market reaction around the result announcement of the 2004 Indonesian presidential election, Siregar and Sianturi conducted a research of LQ-45 and found out that there was no significant difference before and after the result (Siregar and Sianturi, 2005). However, there was a significant difference before and after the cabinet announcement. This research concluded that Indonesia stock market is sensitive to political events.

**H1** = There is an average abnormal return in the stock listed in Kompas-100 around the announcement of candidates in the 2014 presidential election.

### ***Cumulative Abnormal Return around Candidate Announcement***

There was a strong linkage between political uncertainties with common stock returns proven by six events during 2001 until 2006 in Nepal Stock Market (Dangol, 2008). There was an uncertain condition in the 2014 presidential election especially around the announcement of candidates because the voters and investors still had several speculations about the winner and the next economic programs. Therefore, there should be an abnormal return around the candidate announcement.

**H2** = There is a cumulative average abnormal return in the stock listed in Kompas-100 around the announcement of candidates in the 2014 presidential election.

### ***Average Abnormal Trading Volume around Candidate Announcement***

Before the 2004 presidential election, there was a huge increase of trading volume of LQ-45 stock (Anwar, 2004). Candidate announcement is one of the important events during a pre-election period. Then there is supposed to be abnormal trading volume around a candidate announcement to reflect market reaction.

**H3** = There is an average abnormal trading volume in stock listed in Kompas-100 around the announcement of the 2014 candidate presidential election.

### ***Average Abnormal Return around Presidential Election Result***

When the difference in return was expected by the market, we should see the price adjustment when the winner of the election is known (Santa-Clara and Valkanov, 2003). Based on Clara and Valkanov analysis for stock market reaction in the US, when the result of the presidential election is known, stock listed in Kompas-100 in this presidential election is supposed to react in a similar way as reflected by abnormal return.

**H4** = There is an average abnormal return in the stock listed in Kompas-100 around the 2014 presidential election result announcement.

#### ***Cumulative Abnormal Return around Presidential Election Result***

The influence of the election cycle on stock market fluctuations in 52 developing and developed countries since 1994 to 2012 will increase market volatility reflected in the change in the amount of trading and stock return or, on the other hand, it will increase the stock market volatility (Mazol, 2013). It is ensured by Martinez and Santoso, who found out that financial analyst monitoring of political events can be seen in the research of products of investment that constantly ponder over political outcomes (Martinez and Javier, 2003). Based on the logic from those researches, the result announcement of the 2014 Indonesian presidential election is supposed to create a reaction as reflected in the cumulative abnormal return.

**H5** = There is a cumulative abnormal return in the stock listed in Kompas-100 around the 2014 presidential election result announcement.

#### ***Average Abnormal Trading Volume around Presidential Election Result***

When the outcome of the election leads to a change in political orientation of the government, it increases the uncertainty and the investors tend to react in a more volatile manner during a closely contested race (Bialkowski et al., 2006). In the 2014 presidential election, the same conditions took place due to the fact that there was no incumbent. Then the result of the election led to the change in political orientation. As a result, an abnormal trading volume around the result announcement took place.

**H6** = There is an average abnormal trading volume in the stock listed in Kompas-100 around the 2014 of presidential election result announcement.

#### ***Different Reaction Between around the Announcement of Candidate and the Announcement of Winner***

The stock market was bearish in the pre-event period as investors speculated on the election, however, the cumulative return increased in the post period due to the decrease of uncertainty and speculation (Murekachiro, 2013). Although there was uncertainty in the announcement of the result, the level of uncertainty was less than that in the announcement of candidates when the new president had not been not announced yet. This different level of uncertainty created a different reaction.

**H7a** = There is a different average abnormal return in the stock listed in Kompas-100 around the candidate announcement and around the 2014 presidential election result announcement.

**H7b** = There is a different cumulative abnormal return in the stock listed in Kompas-100 around the candidate announcement and around the 2014 presidential election result announcement.

**H7c** = There is a different average abnormal trading volume in the stock listed in Kompas-100 around the candidate announcement and around the 2014 presidential election result announcement.

## **Material and Method**

This type of study is quantitative approach which uses market data such as stock prices and trading data, with measurable data and statistical analysis to test the hypothesis. Therefore, the result of this research is a generalised conclusion. The data used in this study is quantitative secondary data which are stock trading prices and stock trading volume.

### ***Variable Identification and Operational Definition***

This research measures market reaction by abnormal return and trading volume. The first variable is stock price. The stock price used in this research is the closing price for every single day. The second is stock abnormal return or, known as the excess return, is the excess of a realised return with expected return. Abnormal Trading Volume.

Abnormal return, or known as the excess return, is the excess of a realised return with expected return. Abnormal Trading Volume

### ***Type and Source of Data***

The population in this study is published companies whose stock traded in IDX (Indonesia Stock Exchange). The total published companies are 507 companies ([www.idx.co.id](http://www.idx.co.id)). The sample chosen in this study are stocks in group Kompas-100 as it is a group whose stock already fulfilled the criteria of liquidity or traded actively. The detailed criteria of choosing the sample are:

1. Stock listed in Kompas-100 in the estimation and event periods.
2. Have a complete data during the research. Data needed in this research are composite index, daily closing price and trading volume.

### ***Data Analysis Technique***

This research uses a one-sample Kolmogorov-Smirnov test to test the data distribution. Then a significance test is done to test the hypothesis by using one-sample t-test, paired t-test or Wilcoxon signed-rank test. One-sample t-test is used to test each group H1, H2, H3, H4, H5, and H6. The purpose of this test is to know how significant the influence is, or how it contains information about stock return and trading volume, without considering how big the influence is between variables. If the test result indicates significant differences between these variables, it can be concluded that the 2014 Indonesian presidential election contained information that gives impact to stock trading volume and return.

### **Results**

#### ***General Description of Research Subject and Object***

Subjects for this study are companies listed in IDX around the Indonesian presidential election 2014, while the object of this research is market reaction reflected on abnormal return and trading volume. The process of sampling shows that the total member of Kompas-100 index are 100 companies, however, the estimation and event periods of this study equate to three periods of Kompas-100 listing. There are 22 companies that are not listed in Kompas-100 along estimation and event periods, so this study only gets 78 companies as samples.

**Table 1:** Sample Selection Table

<b>Sampling Criteria:</b>	
1. <b>Kompas-100 index</b>	<b>100</b>
2. <b>Not listed in Kompas-100 index during estimation until event period</b>	<b>(22)</b>
3. <b>Does not have a complete data during the research. Data needed in this research are composite index, daily closing price and trading volume</b>	<b>(0)</b>
<b>Final Research Object</b>	<b>78</b>

#### ***Description of Research Result***

The statistical description of this research is used to describe research variables, namely average abnormal return and average abnormal trading volume activity around candidate and result announcements of the 2014 Indonesian presidential election, from the samples of 78 companies listed in Kompas-100 index, from estimation until event period in the forms of maximum, minimum, mean, standard deviation, and variance. Below is the descriptive analysis for each variable.

**Table 2:** Statistical Descriptive

Type		N	MAX	MIN	MEAN	ST DEV
AAR	Candidate Announcement	78	0.0330	-0.4234	-0.0277	0.0467
	<b>Result Announcement</b>	<b>78</b>	<b>0.0867</b>	<b>-0.0896</b>	<b>-0.0013</b>	<b>0.0194</b>
CAR	Candidate Announcement	78	-.1050	.2628	-.001252	.0496458
	<b>Result Announcement</b>	<b>78</b>	<b>.2200</b>	<b>-.1322</b>	<b>-5.14736</b>	<b>.0662117</b>
	Valid N (listwise)	78				
AAR	Candidate Announcement	78	0.13848627	0.0000620	0.007042	0.010342
	<b>Result Announcement</b>	<b>78</b>	<b>0.13657764</b>	<b>0.0000451</b>	<b>0.007554</b>	<b>0.012303</b>

### *Analytical Model and Hypothesis Test*

To investigate whether there are any AAR and AATV, this study uses one-sample t-test. This research uses Mann-Whitney and independent t-test to compare the reaction from the property and real estate sector with the non-property and real estate sector. It uses the Wilcoxon sign-rank test to compare the reaction around candidate and result announcements. Before conducting this hypothesis test, the variables have to meet the data distribution test according to the Kolmogorov-Smirnov test. Based on Kolmogorov-Smirnov test, data distribution is normal if it has a value of more than 5%. Data distribution for hypothesis 7a, 7b, and 7c are not normal because they have value less than 5 %, which are 2,669%, 1,558% and 2,872%, respectively.

**Table 3:** Result Hypothesis Test

Hypothesis	To Test	Method	Variable	Result
<b>H1</b>	Whether AAR exists around candidate announcement of presidential election 2014	One sample t-test	AAR	Significant, value of sig (2-tailed) less than 5% from D-5 until D+5 (0.000)
<b>H2</b>	Whether CAR exists around candidate announcement of presidential election 2014	One sample t-test	CAR	Not Significant (0.824)
<b>H3</b>	Whether AATV exists around candidate announcement of the 2014 presidential election	One sample t-test	AATV	Significant (0.000)

<b>H4</b>	Whether AAR exists around result announcement of the 2014 presidential election	One sample t-test	AAR	Not significant for D-5 (0.08), D-3 (0.345), D-2 (0.385), D-1 (0.950), D (0.077) and D+1 (0.054). Significant for D-4 (0.004), D+2 (0.038), D+3 (0.009), D+4 (0.013), D+5 (0.015)
<b>H5</b>	Whether CAR exists around result announcement of the 2014 presidential election	One sample t-test	CAR	Not significant (0.945)
<b>H6</b>	Whether AATV exists around result announcement of the 2014 presidential election	One sample t-test	AATV	Not significant for D-5 (0.084), D-3 (0.345), D-2 (0.385), D-1 (0.950), D (0.077) and D+1 (0.054). Significant for D-4 (0.004), D+2 (0.038), D+3 (0.009), D+4 (0.013), D+5 (0.015)
<b>H7a</b>	Different reaction between candidate announcement and result announcement	Wilcoxon Sign Rank	AAR	Significant (0.000)
<b>H7b</b>	Different reaction between candidate announcement and result announcement	Wilcoxon Sign Rank	CAR	Not Significant (0.490)
<b>H7c</b>	Different reaction between candidate announcement and result announcement	Wilcoxon Sign Rank	AATV	Not significant (0.589)

## Discussion

This study revealed that the highest value of AAR around the candidate announcement comes from JPFA or non-property and real estate sector with the value of 0.0330 while around the result announcement the highest value comes from APLN which is included in property and real estate sector with the value of 0.0867. The lowest value of AAR around candidate announcement comes from ICBP included in Consumer Goods Industry with the value of -0.4234 while around result announcement comes from BWPT with the value of -0.0896. The average value of average abnormal return from securities listed in Kompas-100 index around candidate announcement of the Indonesian presidential election 2014 is 0.0277 with the standard deviation of 0.0467. It shows that the average of AAR around result announcement is 0.0013 with the standard deviation of 0.0194.

This study also revealed that the minimum value of CAR around candidate announcement is from ADHI with the value of -0.1050 and the highest value is from SSIA with the value of 0.2628. The highest CAR around result announcement is from RALS with the value of 0.22 and the lowest is from BBTN with the value of -0.1322. It means CAR around result announcement is lower than around candidate announcement.

Trading volume activity describes the comparison between trading stock and outstanding stock. An event period of 5 days before up to 5 days after the announcement of candidate creates a statistical average of abnormal trading volume activity, with the mean of 0.007042 and with the standard deviation of 0.010342705, while around result it has the average of 0.00755404 and the standard deviation of 0.00015138. The highest value of AATV around candidate and result announcement comes from BKSL, one of the companies listed in the property and real estate sector. The lowest value around candidate announcement is from the telecommunication company, ISAT. Around the result announcement, the lowest value is from the finance sector, PNBN especially.

From the hypothesis test, there is a market reaction around the candidate announcement reflected by significant AAR and AATV for every single day from D-5 until D+5. However, the cumulative abnormal return around candidate announcement shows a different reaction from either AAR or AATV. CAR around candidate announcement is not significant. The existence of negative AAR around candidate announcement shows that there was a price change inside the Kompas-100 index. The price changes reflected that the investor incorporated available information about the 2014 presidential election candidate into prices. Therefore, they got an abnormal return. It means that candidate announcement of the 2014 presidential election had a strong impact on the stock market. The existence of significant AAR every single day before the candidate announcement, means that there was an information divulgence about the candidate. It confirms previous research conducted by (Liu, 2007) which showed abnormal

return during pre-election period due to the existence of uncertainty in four countries from the sample of five countries.

In accordance with the existence of AAR around the candidate announcement, the existence of average abnormal trading volume per day around the candidate announcement showed that the candidate announcement changed investors' beliefs and induced them to engage in a new round of trade. It is confirmed by (Anwar, 2004) who stated that there was a huge increase of trading volume in the 2014 presidential election. The 2014 presidential election also shows the same reaction by the significant AATV around candidate announcement. The abnormal volume around the candidate announcement is positively correlated with the abnormal return. Then, it can be concluded that IDX is a semi-strong efficient market around candidate announcement because the market quickly reacts in incorporated information about the candidate of the 2014 presidential election.

The hypothesis test around result announcement shows that there are significant AAR and AATV in D-4, D+2, D+3, D+4, and D+5. Significant AAR and AATV in D-4 can be seen as a signal of the result. However, the insignificant amount can be seen in D-3. It can be caused by the profit taking action from investors. Significant AAR and AATV since D+2 until D+5 show that the market started to react from D+2 of result announcement. This result is in line with the research done by (Santa-Clara and Valkanov, 2003). It is said that when the difference in return is expected by the market, a price adjustment would be seen when the winner of election is known. The negative abnormal return can be a signal of bad news. In accordance with price, the trading volume was also significantly different since 2 days after the result announcement. It is assured by Kim and Verrecchia that volume is proportional to price changes (Gao and Oler, 2012; Kim, 2017; Kim and Verrecchia, 1991). Although the reaction started from D+2, it can still be concluded IDX is semi-strong efficient around result announcement.

Unlike the AAR and AATV, there is no significant CAR around result announcement. It can be caused by the different value of AR along the event period. The positive and negative values of AR create the cumulative abnormal return that is close to zero (insignificant). There is no difference between CAR around the candidate announcement and result announcements. It can be caused by the insignificant CAR around the candidate and result announcements. However, there are different AARs of Kompas-100 index around candidate announcement and result announcement. AAR around result announcement is less than the one of candidate announcement. It is ensured by (Bialkowski et al., 2006) that when the outcome of an election leads to a change in political orientation of the government, it increases the uncertainty and investors tend to react in more volatile manner. In the 2014 presidential election, there was no incumbent, the election therefore would lead to a change in political orientation. The candidate announcement had a higher level of uncertainty due to more speculation around the candidate



announcement. It is clear that this was the reason why the abnormal return during candidate announcement was more than the abnormal return around result announcement.

However, AATV is not in accordance with AAR because there is no difference in AATV around candidate announcement compared with AATV around result announcement. Bamber and Cheon explained that nearly a quarter of the result announcements generate very high trading but little price change or large price but little trading (Bamber and Youngsoon, 1995; Dorminey et al., 2018; Fernando et al., 2016). Using the same logic, Bamber and Cheon analysed that heavy trading is relative to price reaction when the announcement generates different belief revisions among individual investors. But a small average of the aggregate market generates belief revision and vice versa.

### **Conclusion**

It shows that there was an information divulgence reflected by significant AAR started from before the official candidate announcement. There is no difference in CAR around the candidate and result announcements while there is a different AAR of Kompas-100 index around candidate announcement compared to around result announcement. However, the AATV shows that there is not any significant difference between candidate announcement and result announcement. IDX is semi-strong efficient during the official candidate and result announcements, but more reactive during candidate announcement rather than result announcement.

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