

The Effect of Financial Reporting Quality, Debt Maturity, Political Connection, and Corporate Governance on Investment Efficiency: Evidence from Indonesia

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This study aims to examine the effect of financial reporting quality, debt maturity, political connection, and corporate governance on a firm's investment efficiency. This study uses quantitative research with multiple linear regression models. The sample employed in this research includes manufacturing and infrastructure companies listed on the Indonesia Stock Exchange (IDX). The type of data used for this study is secondary data in the form of financial statements and annual reports from 2013 to 2016. The sample selection utilises a purposive sampling method with 86 samples of selected companies. This will be analysed over a four-year research period. Therefore, there are a total of 344 observations in the study. The results suggest that financial reporting quality, debt maturity, and corporate governance are positively associated with investment efficiency. However, the political connection is not associated with investment efficiency. This study can be beneficial for the Financial Services Authority, creditors, and investors to improve the efficiency of private sector investment in Indonesia.

Key words: *investment efficiency, financial reporting quality, debt maturity, political connection, corporate governance, private firms.*

Introduction

In a developing country, investment is one of the economic growth determinants. This this can be investment in physical capital or working capital (Dewan & Hussein, 2001). Through investments, various types of production facilities can be provided which creates added value, leading to the growth of a country's economy. An investment can be created by two main sectors in the economy, which are governments and private sectors. Private investment becomes important if the state is unable to provide for the needs of the community. Despite government investment, investments made by the private sector will certainly have an impact on the economy of a country. Various studies on factors that influence private investment in Indonesia focus on macroeconomic variables, such as lending rates, gross domestic product, inflation rates, and government spending. In addition to macroeconomic factors, there are other small-scaled factors in firm levels that has been researched in 2006 by Biddle & Hillary.

In a neoclassical economic environment, managers are given capital to invest until the marginal rate of return is zero (Hayashi, 1982; Jake, 2017, Jake, 2017, Jayathilaka and Purasinghe, 2017, Jiang and Smith, 2017, Johar et al., 2017). However, there are other factors that affect the efficiency of investments made by managers. These factors include the existence of information asymmetry of both managers and investors (Biddle & Hilary, 2006). The existence of factors, other than macroeconomics, that affect investment at the company level provides a novel view that accounting numbers, the company's financial condition, and managerial behavior can influence the efficiency of investment. As stated by Biddle et al. (2009), information asymmetry between a company and capital providers reduces investment efficiency due to the emergence of market friction, comprised of adverse selection and agency cost. Similarly, investment efficiency has become an interesting object to study as it shows the manager's behaviour towards capital owners including creditors.

This study bases its analysis on the perspective of agency theory, defining a company as a collection of contracts (nexus of contracts) that relates between individuals. For example, the relationship between the owner of economic resources (principal) and managers (agents) who take care of the use and control of company's resources (Jensen & Meckling, 1976). Watts & Zimmerman (1990) propose three hypotheses based on the theory in positive accounting theory that explains the existence of three forms of agency problems. The three forms are defined as the relationship between owners and managements, creditors with managements, and government and managements.

The quality of financial reporting is being studied for several reasons. First, financial reporting quality reflects the manager in the company. Second, accurate financial reporting can reduce harmful investment decisions and moral hazards, so that investment opportunities can be better

identified (Lambert, Leuz, & Verrecchia, 2005). Third, research using financial reporting quality as a variable reflects firm-level data.

Another important determinant other than financial reporting quality used in this research is debt maturity. Ortiz-Molina & Penas (2008) stated that shorter debt maturity can reduce problems related to asymmetric information. In the research of Gomariz & Ballesta (2014), it was constituted that debt maturity influenced investment efficiency. For companies with more short-term debt, the effect of financial reporting quality on investment efficiency is higher, compared to companies which own abundant long-term debt. Prior research has emphasized the role of debt maturity as a mechanism that is able to weaken information asymmetry and to reduce agency cost between shareholders, creditors, and managers (D'Mello & Miranda, 2010; Gomariz & Ballesta, 2014).

The results of a study conducted by Chen et al. (2011) found that the sensitivity of investment is higher in state-owned enterprise (SOE) compared to non-SOE. Chen et al. (2011) also found that political connection negatively affected SOE investment efficiency while there was no evidence for non-SOE. The influence of political connection addressed in this research is based on moral hazard models that predict overinvestment due to agency conflicts between managers and shareholders (Chen et al., 2011). According to previous research, political connections will change the functions and objectives of the company to be desired by the government. Political connections represent a connection between a company (managers and shareholders) and government, reflected by the politically connected executives of the company.

The last determinant used in this research is corporate governance which exemplifies a company's commitment to a good corporate management. A general definition of corporate governance is articulated in the Cadbury Report (1992) as a system where companies are directed and controlled. Research conducted by Chen & Chen (2017) stated that investment efficiency is different due to several aspects of corporate governance, such as board characteristics, ownership structures, compensation of directors, and quality of audit committees. The study concluded that capital allocation for investment becomes more efficient with effective corporate governance, both internally and externally (Chen & Chen, 2017). Unlike the previous research, this study uses the corporate governance index to capture the full roles of corporate governance that are not limited to a certain component of governance.

This research is different from previous studies as it uses a model which tests four variables simultaneously. These variables are financial reporting quality, debt maturity, political connection, and corporate governance in one research model. The choice of foretold factors is based on the elements of the company, comprised of behaviour of managers, creditors, and owners of companies represented by the board of commissioners within the scope of agency theory. The four determinants reflect various stakeholders who are interested in the company.

Using indexes of corporate governances is a novel element in this research because it can provide a complete overview of the corporate governance.

This research was conducted to determine the effect of various factors related to the company described earlier. The selection of these variables is based on agency theory regarding problems between managers and shareholders or company owners, between companies and creditors, and between companies and the government.

Hypothesis Development

Agency theory explains that management holds differing perceptions from the owners of companies. The quality of financial reporting represents the function of the manager in the company and becomes an authority of the managers. When the financial reporting quality is poor, asymmetry information problems will arise, whether in forms of excessive selection of cash or the adverse selection of investments. Biddle & Hilary (2006) explain the relationship between the quality of financial reporting and investment efficiency. The results explain that high accounting quality will improve investment efficiency by reducing asymmetric information between managers and outside suppliers. Biddle et al. (2009) conducted additional research to answer investment efficiency issues from the overinvestment or underinvestment point of view. The results of the study indicates that companies with high financial reporting quality are less likely to deviate from the predicted level of investment. Gomariz & Ballesta (2014) state that financial reporting quality is able to reduce investment inefficiency problems.

H_1 = The quality of financial reporting has a positive effect on investment efficiency

In agency theory, a relationship between shareholders and creditors is established. The relationship between the two parties can lead to shareholder-debtholder agency problems because of the asymmetrical information between the two. Existing asymmetrical information can be mitigated by monitoring mechanisms carried out by creditors. Creditors who provide short-term debt will be easier to supervise the company. Therefore, companies with more short-term debt have slight asymmetry information. Gomariz & Ballesta (2014) examined the effect of debt maturity and financial reporting quality on investment efficiency. The result of the study indicates that low debt maturity (more dominant long-term debt) can increase investment efficiency. This study found that financial reporting quality and debt maturity can substitute each other. In addition, Sakti & Septiani (2015) used data for one year in all business sectors. The study showed that financial reporting quality and debt maturity have a positive effect on investment efficiency.

H_2 = Debt maturity has a positive effect on investment efficiency

Public companies can be inefficient due to the political pressures that control the company (Shleifer and Vishny, 1994). Furthermore, this statement was utilised by Shleifer and Vishny (1994) to create The Grabbing Hand Theory, explaining that there are political interferences influencing corporate decision making. Politically connected companies can gain privileges related to the ease of investing in fixed assets or projects. When investment fails, companies get assistances from the government through political connections in order to keep the company going concern. On the other hand, political connections can cause issues in the selection of investments due to the intervention of other parties. Chen et al. (2011) examine the measurements of government intervention at two different levels. First, the study compared SOE and non-SOE companies. Second, the research by Chen et al. (2011) measured government intervention. In particular, whether the company is politically connected through the appointment of top executives who have a background in government. The results showed that political connections significantly reduce investment efficiency on SOE. However, there is no similar evidence found on non-SOE. Companies that experience government intervention invest more than companies that are not intervened (Deng et al., 2017).

H₃ = Political connections have a negative effect on investment efficiency

Chen & Chen (2017) have identified that the efficiency of investment in companies with diversified assets is influenced by several aspects of corporate governance, such as board characteristics or the quality of audit committees. The results of the study shows that purchasing assets from companies with high board independence, low participation of boards in business, and outside company directors are more efficient. The results of the study by Chen et al. (2017) showed that ownership and governance structures play a role in determining investment efficiency in companies. This research consisted was extrapolated from observations on listed exchange companies in China. In prior studies, corporate governance was proxied with only a few components. This study uses a corporate governance index based on all governance components. The use of indexes can capture the function of corporate governance and its effect on efficiency as integral.

H₄ = Corporate governance has a positive effect on investment efficiency

Data and Research Design

Independent variables & Financial reporting quality

A study conducted by Gomariz and Ballesta (2014) stated that there are several proxies that can be used to measure financial reporting quality. In this study, the model used is based on discretionary accruals model developed by Kasznik (1999) which is built upon the previous research of Jones (1991).

$$TA_{i,t} = \beta_0 + \beta_1 \Delta Sales_{i,t} + \beta_2 PPE_{i,t} + \beta_3 \Delta CFO_{i,t} + \varepsilon_{i,t}$$

$TA_{i,t}$	=	Total accruals are calculated as changes in non-liquid current assets less current liabilities plus changes in short-term bank loans less depreciation in company i in year t
$\Delta Sales_{i,t}$	=	Annual change in sales revenue of company i in year t
$PPE_{i,t}$	=	Property, plant, and equipment of company i in year t
$\Delta CFO_{i,t}$	=	Changes in the company's operating cash flows i in year t
$\epsilon_{i,t}$	=	Residual value

Debt maturity

The measurement of the debt maturity variable uses a proxy in the research of Gomariz and Ballesta (2014) which is symbolized by STDebt (short-term debt). Debt maturity is interpreted as a comparison between short-term debt and total debt. The more the company's short-term debt is, the higher the STDebt value and the lower the maturities are.

Political connection

Political connections are measured using a proxy for the presence or absence of a corporate executive connected to the government. A company executive is defined as the board of commissioners and directors of the company. Information about board members can be obtained from the sample company's annual reports, particularly in the background of the board of commissioners and directors section. Determination of a dummy variable valued as 1 (one) in this study correlates with guidelines that have been previously used in research using similar proxies in the Ferdiawan and Firmansyah (2017) study, as follows.

1. if there is one Director or Commissioner who is also a member of the House of Representative, a member of the Executive Cabinet, an official in one of the government institutions including the military, or a member of a political party, or
2. if there is one Director or Commissioner who is also a former member of the house of representative, a former member of the executive cabinet, or a former official in one of the government institutions including the military.

Corporate governances

The corporate governance variable is measured by developing an index comprised of five main measurement dimensions. The five dimensions are: rights of shareholders, equitable treatment of shareholders, roles of stakeholders, disclosure and transparency, and the role of the board of directors in accordance with corporate governance guidelines developed by the OECD. The main dimensions related to governance are then analyzed by indexing using OECD guidance from a scale of 0 to 1. The governance index used is based on research by Cheung et al (2014).

The selected index process uses the unweighted index rule that gives each item the same value according to Neuman (2014, 153).

Dependent variable

Investment efficiency is calculated using a company-specific measurement model. Biddle, Hilary, and Verdi (2009) use investment models as a function of growth opportunities (measured by sales growth).

$$\text{Investment}_{i,t} = \beta_0 + \beta_1 \text{SalesGrowth}_{i,t-1} + \mu_{i,t}$$

Investment = The company's investment in fixed assets measured from capital expenditures to obtain fixed assets reduced by the proceeds of sale of fixed assets and scaled to the total fixed assets of the previous year.

SalesGrowth = Average of the company's sales growth in a year. Sales growth for each company is calculated by $100 \times \Delta \text{Sales}_{i,t-1} / \text{Sales}_{i,t-2}$

M = Residual value

The residual values are estimated cross-sectionally for each study year and for 86 sample companies. Cross-sectional calculations are carried out to assume differences in industry conditions each year and are related to the annual period of financial statements.

Research model

The main model of research is used to find the relationship between financial reporting quality, debt maturity, political connections, and corporate governances that are modelled as follows:

$$\text{InvEff}_{i,t} = \alpha_{0i,t} + \beta_1 \text{FRQ}_{i,t} + \beta_2 \text{STDebt}_{i,t} + \beta_3 \text{Polcon}_{i,t} + \beta_4 \text{CG}_{i,t} + \beta_5 \text{Size}_{i,t} + \beta_6 \text{CFO}_{i,t} + \beta_7 \text{Age}_{i,t} + \beta_8 \text{Tang}_{i,t} + \varepsilon_{i,t}$$

InvEff _{i,t}	=	Investment efficiency
FRQ _{i,t}	=	Financial reporting quality
STDebt _{i,t}	=	Debt maturity
Polcon _{i,t}	=	Political connection
CG _{i,t}	=	Corporate governance
Size _{i,t}	=	Firms size (control variable)
CFO _{i,t}	=	Operating cash flow (control variable)

Age _{i,t}	=	Company listing age (control variable)
Tang _{i,t}	=	Tangible fixed assets (control variable)

Control variables

The control variables used are company size, operating cash flow, tangible fixed assets, and age of company listings. The use of control variables refers to previous research which can explain the variable efficiency of investment. Control variables are not explained in the discussion section. The control variables consider other factors besides the research variable. The choice of company size and operating cash flow are based on research by Gomariz and Ballesta (2014). This research indicates that company size calculated based on sales has a negative effect, while operating cash flow has a positive effect on investment efficiency. Listing age and tangibility variables are based on research by Chen et al. (2010). The age of company listings and tangibility both have a positive effect on investment efficiency.

Samples

Secondary data sources used in this study are financial statements of companies listed on the IDX for the period of 2012 and 2016. The company's 2011 financial position reports are also used to calculate previous period data. This includes lagged total assets and the sales growth of the company for the previous year. The secondary data is taken from the IDX's page <http://www.idx.co.id>, as well as compilation data from The Indonesia Capital Market Institute (TICMI) and Thomson Reuters. Data related to corporate governance is obtained by indexing the company's annual report obtained from the company's website or the IDX website. Samples were chosen based on several criteria. These criteria include companies that carry out IPO before January 1, 2011, have complete data for the period of 2011-2016, submit annual reports in English, and have information related to corporate governance that can be obtained in annual reports. Information from 86 samples of selected companies will be considered over a four-year research period. Therefore, there will be a total of 344 observations in this study.

Results

Descriptive statistics

Table 1 shows descriptive statistics for the variables studied, including the mean, median, standard deviation, maximum values, and minimum values. Investment efficiency (InvEff) has an average value of -4,850 and a mean value of -3,570 which is consistent with previous studies (Gomariz & Ballesta, 2013; Chen, et al., 2010). The negative value indicates a change in the model description from earnings management to financial reporting quality. Debt maturity has an average value of 0.593, which means that more than 50% of sample companies have more short-term debt in their debt portfolio. The average value of political connections indicates that

38.4% of sample companies have political connections. Based on these statistics, sample companies have implemented more than 50% of guidelines related to corporate governance.

Table 1: Descriptive statistics

	InvEff	FRQ	STDebt	Polcon	CG	Size	CFO	Age	Tang
Mean	-4,850	-0,054	0,593	0,384	0,535	1,3x10 ¹³	0,084	18,744	0,410
Median	-3,570	-0,042	0,611	0,000	0,539	2,3x10 ¹²	0,071	21,000	0,397
Maximum	-0,005	-3,5x10 ⁻⁵	1,000	1,000	0,794	2,6x10 ¹⁴	1,025	36,000	0,953
Minimum	-52,375	-0,338	0,003	0,000	0,224	2,9x10 ¹⁰	-0,379	3,000	0,012
Std. Dev.	5,607	0,053	0,314	0,487	0,106	3,1x10 ¹³	0,119	7,502	0,229
Obs.	344	344	344	344	344	344	344	344	344

A Multicollinearity test was conducted to test whether there is a correlation between independent variables. Table 2 is a correlation matrix showing that there is no correlation between research variables. Thus, it can be concluded that this study is free from the problem of multicollinearity.

Table 2: Correlation matrix

	FRQ	STDebt	Polcon	CG	Size	CFO	Age	Tang
FRQ	1,0000							
STDebt	-0,1477	1,0000						
Polcon	-0,0331	-0,0027	1,0000					
CG	0,0855	-0,1755	0,1169	1,0000				
Size	0,1224	-0,3833	0,3054	0,3116	1,0000			
CFO	-0,1280	-0,0010	0,0206	0,0546	0,0813	1,0000		
Age	-0,0434	0,1460	-0,0012	-0,0634	-0,1030	0,0569	1,0000	
Tang	0,0400	-0,2511	-0,1610	0,0605	0,2130	0,0023	-0,2707	1,0000

Regression results

Regression results in Table 3 show the significant influence of the four variables studied. Based on the results of statistical testing, FRQ has a significant positive effect on investment efficiency, showing that financial reporting quality plays an important role in managing the existence of asymmetric information on the company. Regarding debt maturity, STDebt has a positive coefficient, which means that more short-term debt (lower maturity) will increase investment efficiency. The corporate governance supports the other two variables displaying positive effect on investment efficiency. Unlike other variables, political connections show no influence on investment efficiency.

Table 3: Regression on investment efficiency

Variables	Effect	Regression	
		Coefficient	Prob.
FRQ	+	16,4391	0,0018
STDebt	+	2,39538	0,0137
Polcon	-	0,54264	0,2129
CG	+	7,10513	0,0088
Size		0,35603	0,0257
CFO		-4,91664	0,0588
Age		0,90874	0,0541
Tang		-3,60862	0,0074
<i>R-Squared</i>	0,10808		
<i>Adj. R-Squared</i>	0,08678		
<i>F-Statistic</i>	5,07433		
<i>Prob (F Statistic)</i>	0,00001		

Analysis and empirical results

The effect of financial reporting quality on investment efficiency

Based on the results derived from hypothesis testing, it can be observed that financial reporting quality has a positive effect on the efficiency of corporate investment. The quality of financial reporting is closely related to the role of managers including their behaviour. Furthermore, this study is able to explain agency theory where there is a problem with information asymmetry leading to inefficient investments. The quality of financial reporting has a role to reduce asymmetric information, referring to the problem of excessive cash, moral hazard, and improper investment selection (adverse selection). The results generated in this study are in line with the conclusions of Biddle et al. (2009) which found that financial reporting quality has a positive influence on the investment efficiency. Although previous researchers observed all the industrial sectors, a study focusing on the manufacturing and infrastructure sectors could

also provide the same information. This is because the two sectors used (manufacturing and infrastructure) are the most dominant in terms of the number of companies.

This study reviews manager behaviour related to investment efficiency using agency theory. Agency theory can explain how the company's investment becomes inefficient. In this case, there is a problem of overinvestment or underinvestment. Good quality financial reporting can reduce the problem of information asymmetry between financial report makers and users. The quality of financial reporting can represent managerial factors that are closely related to conflicts of interest and the existence of agency problems. The selection of accounting policies, as well as the investment decision on fixed assets, is at the discretion of the manager. The results of this study provide an analysis of managers' behaviour relating to accounting policies, especially policies related to financial statements and investment plans.

The effect of debt maturity on investment efficiency

In accordance with the results of hypothesis testing, debt maturity has an influence on investment efficiency. This research confirms the positive influence between two variables, which explains that the higher amount of short-term debt will contribute to higher efficiency on investments. This research defines one of the agency theories, known as shareholders-debtholders agency problem. It explains that there is an asymmetry information between the two parties that can be mitigated by the supervision of creditors. Greater amount of short-term debt in the company will increase the supervision of creditors including supervision regarding the selection of the right investment. The results of this study are in line with the research of Gomariz & Ballesta (2014), which determined that the debt maturity has a positive effect on the investment efficiency. The research of Gomariz & Ballesta (2014) was conducted in Spain which is a developing country similar to Indonesia. Both Indonesia and Spain are countries where financial markets are still developing, and companies tend to use funding through debt.

Functions of the debt in the scope of agency theory can be explained from companies' point of views as a debtor or a creditor. Debtors choose more short-term debt in debt portfolios to provide information about the company's financial health, while the creditors prefer short-term debt compared to long-term debt for supervisory functions. Rajan (1992) also stated that the use of short-term debt is more appropriate than long-term debt, with the intention to establish a supervisory function for managers. The larger amount of short-term debt gives the creditor a right to conduct more supervision. This will have an impact on the efficiency of the company's investment. Creditors must supervise and maintain whether the loan funds are used properly by the company. The monitoring function carried out by the creditors is able to maintain the behaviour of managers in fixed assets investment and to direct the managers' attention to the returns of their strategic investments.

The effect of political connections on investment efficiency

According to results of this study, political connections do not affect investment efficiency. This result is in line with the research conducted by Chen et al. (2011), which determines that no influence from political connections on investment efficiency in non-SOE. The prior research found that political connections had a negative effect on investment efficiency in SOE, while there is no influence on non-SOE companies. The outcomes of this study are in accordance with Chen et al.'s (2011) findings that government intervention in the form of political connections plays a vital role in SOE through significant ownership, while there are not many registered public companies intervened by the government ownership. The results of this study are not in accordance with the research conducted by Ling et al. (2016). The prior study stated that companies with strong political connections tend to experience problems of overinvestment, meaning there is a negative influence between these two variables. Consequently, the presence of political intervention in companies causes a distortion in resource allocation and may trigger poor performance of the companies.

In this study, there is no finding that explains the influence of political connections on the efficiency of corporate investment. However, it does not mean that there is no influence at all. The effect of political connections is found at the level of corporate funding for investment or operational activities. The research of Khwaja and Mian (2005) cited in the study of Deng et al. (2017), explains that politically connected companies found it is easier to obtain loans from banks. This is used in the investment of fixed assets or in profitable projects. Political connections can be also viewed from the existence of company executives who are still active in the government as officials or are retired. This study found that executives who are inactive outnumber the executives who are still active officials.

Table 4: The composition of executives in politically connected companies

	2013	2014	2015	2016
Total executives in politically connected samples of company	301	306	422	381
The sum of politically connected commissioners	51	46	56	54
The sum of politically connected directors	2	4	4	3
The sum of politically connected executives which is also the active officials	20	10	18	20
The percentage of active politically connected executives compared to total executives	37,74%	20,00%	30,00%	35,09%

The effect of corporate governance on investment efficiency

The results of hypothesis testing determine that corporate governance influences the investment efficiency. The majority of previous research on corporate governance that has been carried out only examines one or few components of governance. In contrast, this study uses an index method to appraise all corporate governance components. Therefore, the results of the previous study show different test results between the components of governance. A study in China that was conducted by Chen, Sung, and Yang (2015) reviewed governance sub-components. The results obtained from that study differ for each of sub-components. For example, ownership concentration has a negative effect, while incentive compensation has a positive effect. This study, however, uses a corporate governance index that combines all components of governance so that the results obtained are able to capture the overall influence of governance. Therefore, this study is able to demonstrate the role of all corporate governance components on the efficiency of corporate investment. This research can be compared to the condition in China because the characteristics of Indonesian and Chinese companies are based on a two-tier board system. The system allows the separation of functions between directors, whose duty is to carry out the company's operational activities, and the board of commissioners, who represent the owner of the company.

Robustness Check

Alternative proxies for measuring financial reporting quality

To test the strength of the model and the accuracy of the research variables, alternative proxies for financial reporting quality are used in statistical testing. There are two alternative proxy measurement measures for financial reporting used. These are the McNichols and Stubben and Kothari models.

$$\Delta AR_{i,t} = \beta_0 + \beta_1 \Delta Sales_{i,t} + \varepsilon_{i,t}$$

The model was introduced by McNichols and Stubben (2008). $\Delta AR_{i,t}$ describes changes in accounts receivable at company i in year t . $\Delta Sales_{i,t}$ represents the change in company sales i in year t . All variables are scaled to the total assets of the previous year.

$$TA_{i,t} = \beta_0 + \beta_1 (1/\text{Total Assets}) + \beta_2 \Delta Sales_{i,t} + \beta_3 PPE_{i,t} + \beta_4 ROA_{i,t-1} + \varepsilon_{i,t}$$

The model preceding McNichols and Stubben (2008) is Kothari's (2005) model. $TA_{i,t}$ is total accrual. $\Delta Sales_{i,t}$ represents the change in company sales i in year t . $PPE_{i,t}$ is the total fixed assets (property, plant, and equipment). $ROA_{i,t-1}$ is the return on assets in the previous period. Results of testing using alternative proxies are shown in Table 5 and indicate the same results as the previous test. Nevertheless, the test using McNichols and Stubben proxies showed no effect of financial reporting quality on investment efficiency. This is possible because proxy

measurements of the McNichols and Stubben model does not take into account the total accrual and fixed assets factors, unlike the Kothari model.

Table 5: The regression results using alternative financial reporting quality proxies

Variables	Regression			
	Coefficient	Prob.	Coefficient	Prob.
FRQ McNichols & Stubben	11,12048	0,0551		
FRQ Kothari			12,3508	0,0037
STDebt	2,071424	0,0311	2,1823	0,0223
Polcon	0,516519	0,2303	0,4161	0,2715
CG	7,628839	0,0063	7,2162	0,0081
Size	0,340355	0,0694	-6,2918	0,0497
CFO	-5,664418	0,0131	0,3669	0,0063
Age	0,948421	0,0572	0,8594	0,0708
Tang	-3,734450	0,0073	-3,8623	0,0049
<i>R-Squared</i>	0,090147		0,104084	
<i>Adj. R-Squared</i>	0,068419		0,082689	
<i>F-Statistic</i>	0,000096		0,000011	

Conclusion

This study examines the agency theories and the effect of corporate governance on the efficiency of corporate investment. In prior studies, the variables that formed the agency theory were examined separately. The results of this study showed that the quality of financial reporting has a positive influence on the investment efficiency of sample companies. This is consistent with previous research in other developing countries. The agency relationship between the company and the creditors is shown through debt maturity. This resulted in the finding that companies with higher proportion short-term debt are able to mitigate the existence of information asymmetry, which can improve investment efficiency. This research also identifies the relationship between the company and the government represented by political connections. The results of the study show that political connections to the company executives did not affect the efficiency of the company's investment in terms of the selection of investments in fixed assets. The corporate governance measurement in indexes shows a positive influence on investment efficiency. The use of index can capture the influence of the corresponding variable in total.

The results of this study contribute to the research literature on investment efficiency and behaviour research in the scope of agency theory. This research also contributes to research related to the corporate governance in Indonesia as there is currently a lack of literature related



to this subject and how it is measured. The results of the study have implications for managers, creditors, companies, and governments in terms of how accounting and economic decisions are taken in investment decisions.

This study has several limitations. Firstly, the corporate governance index score used is based on the company's annual report that has not yet can be confirmed by any other party in Indonesia. Secondly, the proxy for political connections is obtained from information on annual reports and other sources of information that need to be confirmed. There is a possibility that there are company executives who are actually politically connected, but the information cannot be obtained or has not been disclosed. Finally, this study has not used a large enough sample size of state-owned enterprises to capture more accurate political connection information. Researchers can consider the issue for further research.

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