CHAPTER I
INTRODUCTION

1.0 Introduction

This study investigates the factors that affect bond ratings in Property, Real Estate, and Building Construction Companies listed on the Indonesia Stock Exchange (IDX). Therefore, Chapter 1 begins by presenting the research context, issues and problem formulation, and research justification. This chapter explains the objectives, targets, research questions, limitations, and the importance of research in experimental research. This chapter ends with operational definitions of the main terminologies used in the study.

1.1 Background of Study

The capital market, as a market for various long-term financial instruments (securities) that can be exchanged, provides economic and financial activities that can help the economic and financial growth of a country, and also serves as an indication of the success of the country and need to pay more attention to domestic economic indicators. In capital transfer operations, the capital market functions as a liaison between parties who have excess capital (investors) and parties who need money (issuers) (Fadilla Yadinanti, Daud Arifin & Rindi Andika, 2022). The capital market plays an important role in a country's economy because it allows companies to raise funds from investors for development, expansion, and working capital, and the public to invest in financial instruments One of the financial indicators that need to be considered in assessing bond ratings is profitability. Bonds are one type of financial instrument offered in the capital market (Dewi & Utami, 2020).

In the development phase, every company definitely needs a lot of funds. Companies must be ready to face threats in obtaining funds, using funds, and returning funds with a rate of return that is in accordance with the agreement with the funder. The capital market is seen as an alternative for companies in obtaining funds accordance with the agreement. The capital market is also seen as an effective means of accelerating development in a country. With the existence of a capital market that is able to existence facilitate the companies-

companies obtain funds to increase economic activities in various sectors. The capital market is used as a means for companies to increase long-term funding needs by selling shares or issuing bonds (Hartono, 2016)

Bonds are long-term, non-transferable debt instruments that indicate that the bond issuer borrows a certain amount of cash from investors with an obligation to pay interest at certain periods and repay the principal debt at a specified time to the bondholder. Both governments and companies issue bonds. Corporate bonds are seen as more profitable than government bonds, as seen from the higher yields compared to government bonds. Furthermore, corporate bonds are dominated by domestic investors who tend to pay more attention to domestic economic indicators than government bonds, while 38% of outstanding bonds are owned by foreigners, making them more vulnerable to global concerns.(Dewi & Utami, 2020).

Bond investment is an income-based investment that is in great demand by capital holders (investors) because of its fixed income. The principal of the bond generates a fixed income, and interest is paid periodically until maturity. The benefit of bond investment is that the bondholder has the first claim on the company's assets if the company experiences liquidity problems because it has signed a commitment to repay the bond without the bondholder buying. Businesses need more cash, such as bonds, which are easier to obtain.(Risawati, 2020) Bond rating is a scale that measures the level of risk and security of bonds issued by governments or companies and provides information announcements and indications about the danger of the company's inability to pay debts. Bond rating agencies provide investors with information about the level of security of bonds, which is indicated by the company's capacity to pay interest on bonds and principal.(Parulian and Suprihatin, 2020).

In investing in bonds, investors need information about the bonds and the issuing company, especially regarding the issuer's ability to pay its obligations. One indicator that can be used to describe information about bonds is the rating issued by a rating company. A rating company is an independent institution that issues ratings that provide information about credit risk for various bonds as well as ratings for the company itself (general bonds rating). The information gap between issuers and investors can be bridged by rating companies by providing information about a company's credit risk (Nugraha, 2010).

According to Izdihar (2017) Issuing bonds also provides greater freedom to pursue acceptable activities, despite the constraints that are sometimes imposed on bank loans. Banks sometimes impose constraints on companies that agree to different terms, such as not issuing further debt or making acquisitions of companies until their debts are repaid. These restrictions can hamper a company's capacity to conduct business and limit its operating options. Issuing bonds allows a company to raise funds without such constraints.

In the context of Property, Real Estate and Building Construction Companies looking to issue bonds to finance their operations and projects, there is a need to understand and assess the many factors that influence their bond ratings. Bond ratings play a critical role in determining a company's ability to access capital markets and obtain favorable borrowing terms.Issuing bonds also provides greater freedom to carry out acceptable activities., As a result, bond ratings have been assigned by many academics using financial performance. However, the conclusions obtained regarding financial performance indicators as elements determining bond ratings still show many inconsistencies.(Izdihar, 2017).

In the context of Property, Real Estate, and Building Construction Companies that wish to issue bonds to finance their operations and projects, there is a need to understand and assess the many factors that influence their bond ratings. Bond ratings play a vital role in determining a company's ability to access capital markets and secure favorable loan terms. As a result, bond ratings have been assigned by many academics using financial performance. However, the conclusions drawn regarding financial performance indicators as a determinant of bond ratings still show many inconsistencies.(Izdihar, 2017).

Bond ratings are influenced by several factors, including Company size, Company growth, Company liquidity, Collateral, Bond age, Auditor reputation, Leverage, Profitability. Bond ratings indicate the company's ability to pay interest or bond coupons to investors. A high bond rating indicates that the potential for bond default is low. Several things to consider in understanding bonds include Bond tenor, Bond issuer, Coupon payment system, and Market conditions.

One of the financial indicators that need to be considered in assessing bond ratings is profitability. Profitability measures a company's ability to generate corporate profits, sales, certain total assets and profits from equity. Raharja and Sari (2008) stated that the higher the level of profitability of a company, the lower the risk of inability to pay obligations or default. Profitability provides an overview of the extent to which a company is effective in generating profits for the company. Companies with increasing or stable profits are considered to have professionalism in managing funds, assets, debts, capital structures owned so that they are considered qualified to be entrusted with funds by investors in the form of bonds. Bond rating companies assess that companies with high and stable profit levels and are able to minimize losses will be smooth in paying bond installments according to the agreement set with investors so as to avoid payment delays. Profit, gain, net income are important aspects in financial reports that are often or frequently assessed by external parties in analyzing a company's financial condition.

The higher the profitability, the more effective the company is in generating profits so that the company's ability to repay the principal and pay interest is better and its bond rating will be high. The higher the bond rating, the lower the probability of the company's risk of failure to meet its obligations. The profitability ratio connects profit, sales and investment. This ratio measures the company's overall operational performance. Profitability shows the company's income position. Profitability measures the ability of capital invested in total assets to create profits. Companies with high levels of profitability are more likely to generate profits. Investors will definitely analyze the company's profitability before investing. This will give investors a sense of security against losses or default. (risk of default) (Izdihar, 2017).

According to Parulian and Suprihatin (2018) Leverage represented by Debt To Equity Ratio (DER) has no impact on bond ratings. In this study, the average DER for banking companies varies. The usual DER has a lower capacity to meet its responsibilities. This shows that a low debt ratio poses minimal risk to investors, but also indicates that the company's debt is moderate. This is related to the decline in bond purchases by investors, which in turn reduces the company's income, indicating that the company's condition is unhealthy. The company will provide a guarantee of high profits, but the potential for large returns is desired by investors, but investors are not willing to take risks. According toParulian and Suprihatin (2018). Bond ratings are influenced by the size of the company-large companies are less risky than small businesses because small businesses are riskier.

Leverage ratio is a financial ratio that describes the relationship between a company's debt to capital and assets (Sofyan Syafri, 2013). This ratio is used to measure the extent to which a company uses debt to finance its investments. The greater the company's leverage ratio, the greater the risk of company failure. The lower the company's leverage, the better the rating given to the company (Herwidi, 2005).

Bonds in large companies are less risky than small companies (Onji, 2013). In addition, company size can also have a correlation with the level of bankruptcy or failure risk so that it can affect bond ratings. Because total debt and company size have a strong and positive correlation, company size can also be used as a proxy to measure liquidity (Andry, 2005) in (Almilia and Devi, 2007). In general, large companies will provide good ratings (investment grade). In addition, company size can also have a correlation with the level of bankruptcy or failure risk so that it can affect bond ratings.

However, there has been no comprehensive research and analysis on the specific factors that affect bond ratings in Property, Real Estate, and Building Construction Companies. Studies on bond rating performance have not been widely and thoroughly researched. This knowledge gap hampers the ability of Property, Real Estate, and Building Construction Companies to make the right financial decisions and optimize their capital raising strategies.

Based on the background and problems that have been described, the researcher is interested in taking the research title "Factors That Influence Bond

Rating Performance in Property, Real Estate, and Building Construction Companies Listed on the Indonesia Stock Exchange (IDX)"

1.2 Problem Statement

Based on the background of the problems that have been described, the author can determine the formulation of the problem that is made to help achieve the main objectives and targets of the research as follows:

1. Does Profitability Ratio have a significant relationship with Bond Rating Performance?
2. Does Leverage Ratio have a significant relationship with Bond Rating Performance?
3. Does Company Size have a significant relationship with Bond Rating Performance?

1.3 Scope of problem

Researcher limiting the problem in this study so that it can be focused on the discussion that has been determined. The limitation of the problem in this study is a discussion of the factors that affect the performance of bond ratings, namely profitability, debt and company size. This study was conducted onsub-sector Property, Real Estate and Building Construction Company.

Investigating the factors that influence the bond rating performance of property, real estate, and building construction companies listed on the Indonesia Stock Exchange (IDX) can provide important insights into the credit risk dynamics of these companies. However, there are certain limitations that need to be considered.

1. Data Availability and Quality

   One of the main limitations is the availability and quality of data. Obtaining comprehensive and accurate data on property, real estate, and construction companies, especially regarding financial metrics, credit ratings, and market performance, can be challenging. Limited data availability can limit the scope and reliability of the analysis.
2. Sample Size

The number of property, real estate, and building construction companies listed on the IDX may be relatively small compared to other industries. The small sample size may limit the generalizability of the findings and increase the risk of statistical bias or anomalies in the analysis.

3. Industry Specificity

   Factors affecting bond rating performance in the property, real estate and building construction sector may differ from other sectors due to sector-specific characteristics, such as cyclicality, regulatory environment and market dynamics. Generalizing findings from this sector-specific analysis to other industries should be done with caution.

1.4 Research purposes

The general objective of this study is to examine the factors that influence bond ratings in the sub-sector.Property, Real Estate and Building Construction Company.Companies listed on the Indonesia Stock Exchange have specific objectives in this study, namely:

1. To test the relationship between Profitability Ratio and Bond Rating Performance.
2. To test the relationship between Leverage Ratio and Bond Rating Performance.
3. To test the relationship between Company Size and Bond Rating Performance.

1.5 Benefits of Research

Understanding the factors that influence bond ratings for Property, Real Estate, and Building Construction Companies listed on the IDX is very important for researchers, universities, investors, and policy makers.

This research contributes toUnderstanding the variables that affect bond ratings is critical for investors because it allows them to make more informed investment decisions, manage risk effectively, and align their investments with their financial goals. This information allows investors to navigate the bond market with more confidence and achieve their goals. Understanding the factors that affect bond ratings allows investors to more accurately assess the creditworthiness of bond issuers. By considering various risk factors, such as financial ratios, industry conditions, and macroeconomic indicators, investors can gauge the likelihood of bond default and potential loss of principal.

For companies, understanding the factors that influence bond ratings is critical to managing borrowing costs, accessing capital markets, and maintaining financial stability. Bond ratings play a critical role in determining a company's ability to raise funds in the capital markets. Learning the factors that influence bond ratings helps companies understand the criteria used by credit rating agencies to assess creditworthiness. By aligning their financial strategies and operations with these criteria, companies can improve their access to capital markets and attract investors on favorable terms.

1.5.1 To Researchers

This study will provide additional knowledge or insight into bond rating performance for other studies, especially regarding factors that influence bond ratings in Property, Real Estate, and Building Construction Companies. Given the limitations of existing research, there are still many inconsistencies in the results obtained related to financial performance variables as a determining factor for bond ratings. Furthermore, this study can be an inspiration for further researchers who want to study financial performance in other businesses. After all, the same elements that influence bond rating performance can also have an impact on other businesses.

1.5.2 To the University

This research will be contributed as a new reference source for students and beneficial for the university. Those who are interested in conducting similar research in the future may find relevant or important information about the Indonesian capital market in this research. They can use this research guideline to complete this or similar research. They can take the best part of a well-conducted research and improve it, and fix the shortcomings.

1.5.3 To Investors

Understanding the factors that influence bond ratings is critical for investors as it enables them to make informed investment decisions, manage risk effectively, and align their investments with their financial goals. This knowledge empowers investors to navigate the bond market with greater confidence and achieve the outcomes they desire.

1.5.4 To Policy Makers

Policymakers play a critical role in shaping economic and financial stability in their jurisdictions. Understanding the factors that influence bond rating performance is important for policymakers as it enables them to make informed decisions and implement policies that promote economic growth, investment and financial stability.