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Analysis of the Effect of Liquidity Ratios, Solvency and Activity on the Financial Performance of the Company (Literature Review of Corporate Financial Management)

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Abstract: This article reviews the influence that aims to really know about liquidity ratios, slovability, and activities that affect the company's financial performance. Liquidity is proxied by *current ratio* (CR), solvability is proxied by *debt to equity ratio* (DER), activity is proxied by *inventory turnover* (InvTO) and *total asset turn over* (TATO), while the company's financial performance is proxied by *return on equity* (ROE). This article was written in order to determine the hypothesis of the influence between variables that can be used in subsequent research. The results of *the library research* are: 1) *Current ratio* (CR) separately affects return *on equity* (ROE); 2) *Debt to equity ratio* (DER) has a separate impact *on return on equity* (ROE); 3) *Inventory turn over* (InvTO) has a separate effect *on return on equity* (ROE); 4) *Total asset turn over* (TATO) has a partial impact *on return on equity* (ROE); 5) CR, DER, InvTO, TATO simultaneously have a positive effect on ROE.

Keyword: CR, DER, InvTO, TATO

INTRODUCTION

The business world is increasingly experiencing intense competition, especially since the emergence of a free trade system in a country. Indonesia is included as a country that gives permission to free trade. This increasingly competitive competition triggers companies to optimize resource in order to obtain organizational goals. The company aims primarily to obtain the maximum level of profit. Companies that are able to show optimal advantages and gain a high market share can have a good impact on the company, especially from the company's financial sector. The profits obtained will have a positive impact on the company's financial performance.

That's why companies need to evaluate the performance of their company's development gradually. Companies are required to be able to determine performance in order to be able to guarantee the sustainability of life. Financial performance as a representation of the achievement of the success of an enterprise, which can be understood as the result obtained from various activities that have already been implemented. Companies need to be able to maximize financial performance to handle increasingly fierce competition in order to maintain a competitive advantage (Mayasari & Al-musfiroh, 2020).

Evaluation of financial performance of companiesn aimed internally or externally. For the company's internal parties to control, coordinate and plan the company in the future. By lysing a financial report, the company's knowledge is for the management to know the position and financial performance, as well as the financial strength in a company. For external parties, it is beneficial for the benefit of investors and creditors. For investors to determine whether to invest or not. As for creditors, it is useful to assess whether the company can pay the amount of money owed when it matures.

Because it is very important to evaluate financial performance so that it is quite wise if from the beginning the company records its finances regularly. With this analysis of financial performance, certain formulas and finances are calculated, so when comparing them with historical and industrial matrices, it will provide knowledge about the situation and financial performance of such enterprises. During the calculation of financial performance, the financial ratio is the most important ratio that is often used in the business world in order to support and improve company performance (Dewa Putu Yohanes Agata, 2021).

Performance in a company can be seen through the company's capabilities as long as it meets its short-term obligations utilizing liquidity ratios. The liquidity ratio acts as the capacity of a company as long as it meets the short-term needs of all three payments due. This ratio is represented using *the current ratio* (CR). This current ratio is a measuring tool for the company's ability to pay short-term obligations or debts that are almost due.

The company's capital structure can come from external, namely the amount of capital received from sources outside the company such as investments and creditors, and can come from internal, namely the amount of capital from sources within the company. Capital structure has a vital role in financial performance in order to develop the company as seen from the source of financing. Solvabiltias ratio is a parameter to show the company's ability to manage short-term financial obligations or short-term financial capabilities (Artaningrum *et al*.., 2017).

Similarly, to measure the company's performance ability can be seen through the activity ratio as a parameter of the company's capabilities while using the company's sources of funds, especially company assets efficiently for business success. The projected activity ratio uses *total assets turn over* (TATO) or referred to as total asset turnover. TATO is a medium for measuring the total number of assets that a company uses in sales activities. The increasing number of company TATTOOS, the company maximizes as long as it uses the company's assets efficiently and can increase sales (Wahyuni & Suryakusuma, 2018).

LITERATURE REVIEW

According to the explanation above, the formulation of the problem to be reviewed in order to be able to design a hypothesis in the next study, includes:

1. Does CR partially affect ROE for a company's financial performance?
2. Does DER have an individual impact on ROE on a company's financial performance?
3. Does InvTP have an individual impact on ROE for the company's financial performance?

4. Does TATO have an individual impact on ROE on a company's financial performance?
5. Do CR, DER, InvTP and TATO simultaneously influence ROE for the company's financial performance?

RESEARCH METHODS

The objectives of this study are:

1. Figuring out CR separately impacts ROE
2. Find out how much DER separately impacts ROE
3. Find out how much InvTO separately impacts ROE
4. Finding out how much TATTOOs separately impact ROE
5. Find out how much CR, DER, InvTO, TATO simultaneously impact ROE

FINDING AND DISCUSSION

Financial Statements

Hongren and Horrison (2017:25) emphasize that financial statements as company documents that submit company reports into monetary terms that provide information in order to provide assistance to insiders determining business decisions based on that information. The preparation of financial statements intends to be able to meet various related parties and management as a benchmark in determining decisions for the next period. Dapat it is said that, the financial statements make it clear about the performance of the company in one period. Information regarding performance is needed in order to determine changes related to efforts tocontrol economic resources in the future and is useful for ensuring the company's capabilities in creating backlog of resource availability.

Financial Performance

Fahmi (2013: 237) explained that financial performance is an analysis to see how far the company has implemented regulations related to financial implementation appropriately. Financial performance pays attention to the financial statements that the company or business entity has, and is represented through information obtained by the balance sheet, profit/loss statements, and all something that participates in supporting to strengthen that assessment of financial performance.

Munawir (2012:31) emphasized that the purpose of measuring a company's financial performance is to: 1). Find out the level of liquidity in order to show the company's capabilities as long as they meet financial obligations that they quickly complete when billing is carried out; 2). Find out the level of solvency in order to be able to show the company's capabilities while fulfilling financial obligations if a company is liquidated, either financial for a short or long period of time; 3). Find out the level of rentability or it can be known as profitability to show the company's capabilities while creating profit value over a certain period of time; 4). Finding out its stability to show the company's ability to run a business consistently, then measurably using considerations of the company's capabilities so that it can pay its debts, and paying interest expenses from debts according to the specified time.

There are various measures of financial performance that companies can use, namely being able to use profitability ratios. This ratio is appropriately used to determine the company's performance which is seen through asset utilization or capital availability because assets and capital are the most important elements for the company's operations.

Financial Statement Analysis

Cashmere (2016:66) said that the analysis of financial statements, namely the number of assets, liabilities/debts, and capital on the company's balance sheet. furthermore, it will also find out the amount of income obtained and the nominal budget of funds used for a certain period of time so that it can find out the results of the profit / loss obtained for a period of time.

Financial Ratio Analysis

Ratio analysis, which is a medium of financial analysis that is often used: in calculating this ratio using a simple arithmetic calculation that can be understood. Each ratio count is more useful than the results of the previous period ratio calculation (Hery, 2012). Harahap (2015:297) states financial ratios as numbers obtained through comparisons between significantly related financial posts.

So it can be concluded that the analysis of financial ratios is an analysis that represents two or several financial data. Financial ratio analysis is useful for establishing the financial health of the company in the current or future. Through this financial ratio, the financial situation and performance of the company in a certain period of time can be disclosed. The purpose of analyzing this ratio, which is to establish the level of liquidity, solvency, effectiveness of operations as well as the level of profitability of an enterprise.

Financial Ratio Analysis Intends to Know the Company's Financial Performance

A company can be called healthy if it is able to survive in any economic situation, seen through the ability to fulfill financial obligations and carry out operations stably and maintain sustainability business development. The performance of the company is the result of stages at the expense of various resources. Performance indicators can be determined through profit. Company profits are needed for the sustainability of the company as well as the company's inability to obtain profits that can result in the company being eliminated from competition in the economic field.

In order to make a profit, it requires the company to carry out its operations which are supported by the availability of decent resources. Profit (net income), which is economic benefit that increases during one accounting period in the form of income or increase in assets or decrease in liabilities, resulting in increased equity not obtained through the investment profit and loss statement, which contains the profit or loss that the company experiences as the main financial statement to convey the results of the company's activities during the profit on a certain period.

Liquidity Ratio

Liquidity ratio is a ratio to show the company's ability to meet financial obligations with an appropriate time frame (Utami and Pardanawati, 2016). That way, if the company has a high liquidity, it means that the company is able to repay their short-term debt. The company will also be more effective in creating profits and financiers will trust the company as a place to invest in it. Companies are also able to create their current assets to meet the needs of the company, so there are not many budget funds that are not useful.

Hantono (2016) states *the current ratio* as a comparison to determine how far current assets cover current liabilities. The greater the comparison of current assets and current debt, the higher the company's ability to cover short-term liabilities. The low *current ratio* is often assumed to be able to show problems in liquidation. It is different if the *current ratio is* too high so that it is not considered good because it shows a large amount of idle funds and causes the company's profitability to decrease.

Solvency Ratio

The company's solvency shows the company's ability to fulfill all obligations if the company isilliquidized. Cashmere (2014:150) mentions if the solvency ratio as a comparison to determine how far the company's activities are funded by debt. A company is considered solvable when the total assets or wealth are insufficient in paying all debts.

Arief Sugiono and Edy Untung (2016:57) said that the solvency ratio is a ratio to determine how far spending is organized by debt and compare it with capital, as well as its ability to pay interest and other fixed expenses. *Debt to equity ratio* (DER) is the ratio of debt appraisers to equity. In order to be able to find this ratio, that is, a comparison between all debts, including current debt and all equities. The value of DER is quite influential in the acquisition of profits that the company gets. The higher the DER, it will show how much trust from outsiders, and this matter provides an opportunity to maximize the company's financial performance because through this large capital, it means that the opportunity to get a profit level is also increased.

Activity Ratio

Activity ratio is a ratio to determine the effectiveness of the company while using the assets that the company has. It can be said that this ratio is useful for determining the level of efficiency in utilizing the company's resources (Cashmere, 2017:172). The activity ratio represents the company'sability to use the assets it owns to earn income from sales (Dermawan and Djahotman, 2013:38). This ratio examines a variety of assets, further establishing the level of activity of that asset at a certain level (Hanafi, 2014: 76).

Comparison of the ratio of activity to each sale with the level of investment in assets in one period so that there is a balance according to the seller's wishes with assets, for example in current assets or other fixed assets. This ratio aims to maximize the company's capabilities while utilizing the assets they own

Through this research, the ratio of activity represented by *inventory turn over* (InvTO) and *total asset turn over* (TATO);

1) *Total assets* turn over, which is a ratio to determine the turnover of all assets in the company, as well as determine the total sales found in each asset (Cashmere, 2018:185).
2) *Inventory turnover*, which is a ratio to determine the amount of costs invested in rotating preparations over a certain period of time. It can also be understood if the rotation of the preparation is intended to show the replacement of the number of prepared goods for one year (Cashmere, 2014: 180)

Profitability Ratio

Profitability is a medium to examine management performance, the level of profit that is able to represent the company's profit position. Financiers in the capital market will certainly pay close attention to the company's capabilities as long as it maximizes profits, which is an attraction for investors to trade shares. On that basis, management needs to be able to meet the goals that have become common targets. Profitability or profit level is a picture of the company's capabilities during the creation of profits through investment.

Profitability indicators can be utilized through comparison of various elements of financial statements, especially balance sheets and profit and loss. Sizing can be carried out in different business cycles with the aim of observing business development (increase/decrease) in a certain period of time, as well as determine the factors behind the company.

The profitibility ratio according to Fahmi's presentation (2014:58) is useful in order to show the company's success while creating profits. The profitability ratio determines the effectiveness of management in paying attention to the results obtained related to sales or investment (Fahmi, 2014: 80). Financial performance can be determined by the measure using *return on equity* (ROE), which measures the ratio of post-tax net profit to equity. ROE analyzes how far companies take advantage of the resources they have in profiting over equity (Fahmi, 2014:82).

If the company has a high level of ROE, it means that the company is performing quite well in financials. This makes it clear that the company's profitability level is high, meaning that the company's capabilities as long as it gets the profit provided to shareholders are increasing.

Table 1. Past Research

No	Research (Year)	Research Title	Result
1.	Sari Puspitarini (2019)	Analysis of the effect of Liquidity, Solvency and Activity Ratios on the Company's financial performance	Based on the results of the study obtained the results of: Simultaneously, a statistical count was obtained that showed CR, DER, InvTO, TATO and SIZE had a significant effect on ROE in consumer industry goods sector companies on the IDX from 2011 to 2013
2.	Dwi Putri Esthirahayu Siti Ragil Handayani Raden Rustam Hidayat (2014)	Effect of Liquidity Ratio, Leverage Ratio and Activity Ratio on Company Financial Performance	According to the description obtained, then: CR, DER and TATO affect together on ROI. CR, DER, TATO affect simultaneously on ROE. CR, DER, TATO affect individuals on ROI. CR, DER and TATO affect individuals on ROE.
3.	Lely Diana Maria Stefani Osesoga (2020)	Effect of Liquidity, Solvency, Asset Management and Company Size on Financial Performance	According to the results obtained, then: Variables of liquidity, solvency, asset management and company size simultaneously have a significant impact on financial performance (ROA)
4.	Sulthon Badar Al Rahman Said Suselo (2022)	Effect of Liquidity, Solvency, and Activity on Financial Performance in Pharmaceutical Companies Listed on the IDX	According to the results obtained, then: CR without meaningfully affecting financial performance. DAR, TATO affects quite meaningfully on financial performance
5.	Henny Anita Siallagan Fatcha Ukhriyawati Chess (2016)	Effect of Liquidity, Solvency, and Activity on Financial Performance in Cigarette Companies Listed on the Indonesia Stock Exchange in 2010-2014	Based on the results of the study obtained the results: CR, DER, TATO influence positively and meaningfully on financial performance
6.	Alma Aprilia Nina Woelan Soebroto (2020)	Analysis of the Effect of Liquidity Ratio, Operating Efficiency, and Solvency Ratio on Financial Performance at PT Bank Maybank Indonesia Tbk for the 2010-2018 Period	Based on the results of the study obtained the results: 1) The comparison of LDR variables, operating costs to operating income (BOPO) and CAR simultaneously affects the ROA. 2) The *variable loan to deposit ratio* (LDR) individually affects the negative and meaningless roa 3) Variable operating costs compared to BOPO individually affect negatively and meaningfully on ROA 4) Car variables individually affect negatively and meaningfully on ROA

7.	Sulthon Badar Al Rahman Said Suselo (2022)	Effect of Liquidity, Solvency, and Activity on Financial Performance in Pharmaceutical Companies Listed on the IDX	According to the results of the study, the results were obtained: 1) The measurement of the ratio of limmunity using CR shows without any significant influence on financial performance 2) Measurements of rasio solvability using DAR show when it affects significantly on financial performance 3) The measurement of the solvency ratio using TATO shows that it affects financial performance.
8.	House Grediani Evieana Saputri Hanifah (2022)	Analysis of the Ratio of Solvency, Liquidity, and Activity to the Performance of Companies in the Trading Sector Listed on the IDX for the 2016-2020 Period	According to the results obtained, then: DAR, CR and TATO have a significant impact on ROA. However, together the variables DAR, DER, CR and TATO affect the ROA in the trading sector contained in the IDX for the 2016-2020 period
9.	Amirudin (2022)	Analysis of solvency and activity ratio to financial performance in PT. HERO SUPERMARKET Tbk period 2011-2021	Results are obtained when: 1) Individually DAR affects meaningfully for NPM 2) Individually TATTOOS do not affect meaningfully for NPM 3) Simultaneously, both DAR and TATO affect the NPM
10.	Irdha Yusra (2016)	The Ability of Liquidity Ratios and Solvency in Predicting Company Profits: An Empirical Study on Telecommunications Companies Listed on the IDX for the period 2007-2014	According to the results obtained, then: 1) The liquidity ratio represented by the *quick ratio affects* positively although not meaningfully for the profitability represented by ROE 2) The solvency ratio*proxied* by dar affects both positive and meaningful for the profitability ratio represented by ROE. This means that it can be used in predicting the company's profit
11.	Rendi Maulana Yusuf Sakti Alamsyah Acep Suherman (2022)	Effect of Liquidity and Solvency Ratio on Financial Performance in the Textile and Garment Sub-Sector (Manufacturing Companies listed on the IDX for the 2017-2020 Period)	Results are obtained when: 1) L ratioof immunity without affecting financial performance 2) Liquidity ratio without affecting financial performance 3) Solvability ratio (DAR) negatively impacts financial performance 4) Liquidity and solvency ratios have a significant impact simultaneously on financial performance
12.	Angga Hendra Saputra Lisdawati (2019)	Effect of *Leverage* Ratio and Liquidity Ratio on the Company's Financial Performance in PT. Wijaya Karya (Persero), Tbk period 2008-2018	Results are obtained when: 1) Individually *leverage* ratio without affecting the company's financial performance 2) Individually the liquidity ratio affects financial performance 3) Simultaneously, *the leverage* ratio and liquidity ratio affect financial performance (ROA)

13.	Faldy G. Lumentut Marjam Mangantar (2019)	Effect of Liquidity, Profitability, Solvency and Activity on Manufacturing Companies listed on the Kompas100 Index for the 2012-2016 Period	Results are obtained when: 1) Liquidity or profitability partially without meaningfully affecting the value of the manufacturing company 2) Solvency and individual activity affect the value of the manufacturing company 3) Liquidity, profitability, solvency as well as activities simultaneously affect the value of manufacturing enterprises
14.	Wiwin Princess Rahayu Dani Sopian (2017)	Effect of Financial Ratio and Company Size on Financial Distress (Empirical Study on Food and Beverage Companies on IDX Period 2013-2015)	Results are obtained when: *1)* The F test results show that liquidity, leverage, growth, and company size simultaneously affect financial *distress.* *2)* Liquidity individually affects positively meaninglessly for *financial distress.* *3)* Leverage individually affects negatively meaningless financial *distress.* *4) Sales growth* individually affects positively meaningful financial *distress.* 5) The size of the company individually affects positively meaningless for *financial distress.*
15.	Enda Noviyanti Simorangkir Trecya Wijaya Cindi Yosi Olivia Naibaho Melvi Amelia Princess (2022)	Effect of Financial Ratio on Financial Kinerja on Food Subsector Companiesin 2016-2020	Results are obtained when: 1) Liquidity variables and activity variables partially without affecting the growth of profits in the food subsector enterprises. 2) The variables of leverage and profitability separately affect the growth of the company's profits. 3) Leverage, liquidity, activity and profitability together affect the growth of the company's profits

Writing Methods

This writing method uses quantitative methods and literature reviews. Through qualitative research, literature review needs to be utilized consistently through methodological assumptions. The factor behind researchers to carry out qualitative studies is that the study is exploratory in nature, (Ali & Limakrisna, 2013).

Discussion

Referring to previous theoretical studies and research, the reviews in this article are:

Free Variables Affect Bound Variables

***Current Ratio* (CR) Memengaruhi *Return on Equity* (ROE)**

CR causes both current assets and current debt to change, changing the level of liquidity as well. If the liquidity value is too high, it will have a bad impact on *the earnings power* because there is *idle cash* or shows the advantages of working capital needed. This advantage can minimize the opportunity to make a profit. On that basis, it is quite possible that the opportunity between CR and ROE is negatively related. The higher the CR, the lower the ROE; comparison between the level of profit and liquidity (Siregar, 2012). According to the explanation, it makes clear the conclusion related to CR, that is, if the CR value is too high or the CR value is too low, it will affect the level of profit. CR has a positive impact on the financial performance of companies represented by ROE.

***Debt to Equity Ratio* (DER) Memengaruhi *Return on Equity* (ROE)**

DER affecting ROE can be seen through Du Pont's model. Du Pont's analysis can evolve again by listing the elements of financial leverage utilization. It seems that in order to maximize the value of ROE in a company, there are various options, namely an increase in financial leverage so that it also triggers an increase in debt (Hanafi, 2014: 88).

***Inventory Turn Over* (InvTO) Memengaruhi *Return on Equity* (ROE)**

The higher this ratio, it means that the more efficiently the company manages its inventory (Rpss et.al, 2009: 86). The larger the *inventory* rotates, the faster the company's cash rotates, and the greater the number of company sales with a slowing InvTO. On that basis, it is quite possible if the relationship between InvTO and ROE is positively related. Due to the increasing size of InvTO, all inventory is more efficient to support sales activities.

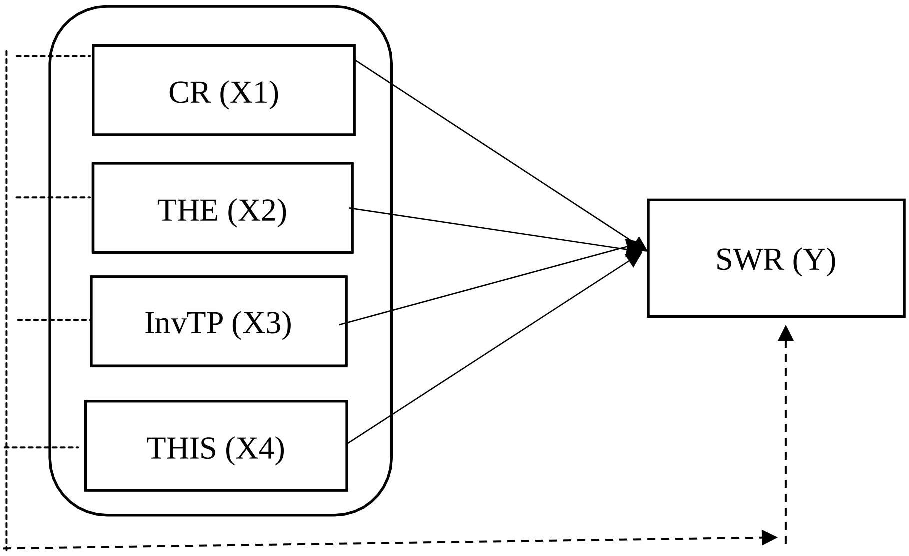
***Total Asset Turnover* (TATO) Memengaruhi *Return on Equity* (ROE)**

TATO is a comparison to describe the measured turnover of assets through sales capacity over a period. The greater the activity ratio, the better so that the asset can spin quickly and make a profit. These results show the increasingly efficient utilization of all assets to create sales (Ardiatmi, 2014). This ratio determines how far the company is able to create sales based on its fixed assets. The activity ratio shows how far the effectiveness of the company is utilizing fixed assets. The higher this ratio, the more effective the utilization of fixed assets (Hanafi, 2014: 78).

TATO is affected by sales and total assets, either current assets or fixed assets. On that basis, TATO can be improved through the addition of assets so that sales can increase. High ratios often indicate good governance. On the other hand, if the ratio is low, then triggering managers need to improve marketing strategies as well as capital use.

Theoretical Framework of Thought

Based on the explanation above, the researcher attaches a frame of mind as described below.



Information:
X1: *Current Ratio* (CR)
X2: *Debt to Equity* (DER)

X3: *Inventory Turn Over* (InvTO)
X4: *Total Asset Turn Over* (TATO)
Y: *Return on Equity* (ROE)

CONCLUSION AND RECOMMENDATION

Conclusion

Based on the above explanation, it can be concluded if:

1. CR separately has a positive and meaningful impact on financial performance as a representative of ROE.
2. DER separately has a positive and meaningful impact on financial performance as a representative of ROE.
3. InvTO separately has a positive and meaningful impact on financial performance as a representative of ROE.
4. TATTOOS separately have a positive and meaningful impact on ROE.
5. Simultaneously obtained CR, DER, InvTO, TATO have a significant impact on ROE.

Suggestion

Based on the explanation above, the advice in this review is that there are still other factors that affect the financial performance represented by ROE, apart from CR, DER, InvTO, TATO. According to the presentation, a follow-up analysis must be carried out in order to get factors that are likely to be able to influence the trust or decisions of managers in evaluating company performance.

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