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Good Financial Reporting Quality, Investment Efficiency, and the Role of Indonesia Sharia Stock Index (ISSI) as a Moderating Variable

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Abstract

The objective of this research is to assess the effects of good financial reporting quality on investment efficiency and the roles of Indonesia Sharia Stock Index (ISSI) as the moderating variable. Here Panel Data Regression Statistics Analysis and Moderated Regression Analysis (MRA) are incorporated. The research population is all companies listed on the Indonesia Stock Exchange (IDX) during the 2019-2021 period, excluding financial-sector companies, and the samples were selected using purposive sampling technique. The results of the analyses provided empirical evidences that good financial reporting quality increases the investment efficiency and that Indonesia Sharia Stock Index (ISSI) as the moderating variable enhances the positive effects of the good financial reporting quality on the investment efficiency

Keywords: Good Financial Reporting Quality; Investment Efficiency; Indonesia Sharia Stock Index

1. INTRODUCTION

National investment realization has consistently increased in recent years. Based on data from the Investment Coordinating Board (BKPM), investment realization in Indonesia continues to increase from Rp 612.8 trillion in 2016 to Rp 1,207.2 trillion in 2022 (bkpm.go.id, 2022). However, the increase in investment realization was not followed by a decrease in the value of the Incremental Capital Output Ratio (ICOR). Indonesia's ICOR scores from 2018 to 2022 were recorded at 6.72, 6.88, -15.09, 8, and 6.22, respectively.

Philippines' ICOR score was (3.7); Vietnam's (4.1); Malaysia's (5.4); and Thailand's (4,4) (Sipahutar, 2023). In comparison, Indonesia's ICOR score in 2019 was 6.88, much higher than that. The higher the ICOR value, the more inefficient a country is for investment (pu.go.id, 2019).

Investment activity is a determining factor for economic growth in developing countries (Al 'Alam & Firmansyah, 2019). With the aim of creating a "conducive investment climate", Indonesia has enacted the Job Creation Law Number 11 of 2020 (Omnibus Law) which aims to encourage increased investment by supporting investment ease and increasing employment (bkpm.go.id, 2021). The simplification of regulations related to investment contained in these regulations is expected to reduce the value of the national ICOR, thereby creating investment efficiency.

The condition of investment inefficiency is related to the agency theory put forward by Jensen & Meckling (1976). In this theory, agency conflicts arise because of information asymmetry between agents and principals. Information asymmetry is a factor that affects company investment because it will make investment decisions less qualified so that the initial goal of investment is not achieved, namely increasing the welfare of shareholders (Sari & Suaryana, 2014). Investment efficiency can be realized if the company does not invest excessively (including investing in projects that have a negative Net Present Value (NPV) and avoids passive activities to invest in projects that have a positive Net Present Value (NPV) (Verdi, 2006; Biddle et al., 2009; Nathaniel & Butar, 2019; and Fajriani et al., 2021).

Higher-quality financial reporting is proven to increase investment efficiency (Ardianto et al., 2021; Biddle et al., 2009; Chen et al., 2011; Gomariz & Ballesta, 2013; and Shahzad et al., 2019). Different results were obtained by Umiyati & Riyanto (2019), who stated that there was no effect on the quality of financial reporting on conditions of investment inefficiency, namely overinvestment and underinvestment. The results of research by Sari & Suaryana (2014) and Handayani et al. (2016) stated that higher-quality financial reporting is proven to reduce underinvestment, but not proven to reduce overinvestment. Following analysts has also not been shown to moderate the relationship between financial reporting quality and investment efficiency.

Currently, Indonesia occupies the position as the country with the largest Muslim population in the world, with 12.7% of the world's Muslim population being Indonesians (worldspopulationreview.com, 2023). The data shows that Indonesia has enormous potential for the development of the Islamic capital market industry, including Islamic

stocks. This was also supported by an increase in the number of Sharia Shares from 2011, namely 252 Sharia Shares, increasing to 552 Sharia Shares by the end of 2022. The market capitalization value of Sharia-based stock indices such as the Indonesia Sharia Stock Index (ISSI) also increased from Rp 1,968,091.37 billion (in 2011) to Rp 4,786,015.74 billion as of December 2022 (ojk.go.id., 2023). The improved performance of the Islamic capital market in Indonesia can also be seen through the award received by the Indonesia Stock Exchange (IDX) from the Global Islamic Finance Award (the most prestigious award in the global Islamic capital market industry) as The Best Islamic Capital Market Award for four consecutive years during 2019 – 2022 (gifaawards.com, 2023). Therefore, this research is interesting to do because Indonesia has investment realization that continues to increase, accompanied by growing conditions in the Islamic capital market industry, but Indonesia's economic conditions are still not efficient because the ICOR value is relatively high.

The results of this study contribute to agency theory which is used to explain the effect of company status listed on the Indonesia Sharia Stock Index (ISSI) and the effect of the quality of financial reporting on investment efficiency. These results can also be input for companies to improve the quality of their financial reporting. The screening carried out by the Financial Services Authority (OJK) of companies listed on the Indonesia Sharia Stock Index (ISSI) is expected to reduce speculation and manipulation that can lead to investors' misjudgments and is expected to become input for policymakers to establish regulations that promote investment efficiency through improving the quality of financial reporting and supported by honest and fair Sharia capital market regulations.

2. LITERATURE REVIEW

2.1 Theoretical Background and Hypothesis Development

An agency relationship is a contract in which the principal (shareholder/investor) engages the agent (company manager) to perform work on behalf of the principal by delegating decision-making to the agent. Agency problems occur when agents and principals both want to maximize their utility, but agents tend to have more information than principals, so it is assumed that agents do not always act in the interests of principals (Jensen & Meckling, 1976; Bushman & Smith, 2001). Information asymmetry affects investment because it will make investment decisions less qualified so that the initial goal of investment is not achieved, namely increasing the welfare of shareholders (Sari & Suaryana, 2014). The existence of information asymmetry between agents and principals can provide opportunities for agents to carry out earnings management in order to

overcome principals regarding the company's economic performance (Ujiyantho & Pramuka, 2007).

According to Bushman & Smith (2001); Hope & Thomas (2008); and Healy & Palepu (2001), one way to resolve agency conflicts between managers and external investors is by improving the quality of financial reporting and disclosure of corporate financial statements. Sharia provisions serve as guidelines for companies whose shares are registered in the Sharia Securities Register (DES) and regulate prohibitions on transactions, activities, and types of business that are contrary to Islamic law (containing elements of usury, mitigating and processing so that it is expected to reduce adverse selection and moral hazard) and improve investment efficiency.

2.2 Good Financial Reporting Quality and Investment Efficiency

The assumption of self-interested behavior in agency theory underlies the unequal desires, motivations, and utilities between management and shareholders. These differences raise the possibility of management behaving unethically by harming shareholders and resulting in low earnings quality (Rachmawati & Triatmoko, 2007). The adverse selection causes managers who have more information than shareholders to overinvest if they decide to sell securities too expensive with the aim of obtaining excess funds (Biddle et al., 2009; Myers & Majluf, 1984). Whereas underinvestment occurs when managers who have more information and act in the interests of old shareholders (old shareholders) may refuse to issue shares at a price discount even though the consequence is the loss of good investment opportunities (Myers & Majluf, 1984). Under moral hazard conditions, managers invest in projects with a negative net present value when there are differences in the interests of managers and shareholders (Biddle et al., 2009).

Verdi (2006); Biddle et al. (2009); Chen et al. (2011); Gomariz & Ballesta (2013); Shahzad et al. (2019); and Ardianto et al. (2021) stated that the higher quality of financial reporting is proven to increase investment efficiency through reducing information asymmetry. According to Handayani et al. (2016), the quality of financial reporting is considered to be better able to describe company information so that it can help companies obtain financing in order to make potential investments. Quality disclosure through transparent reporting of financial information reduces the tendency of managers to issue securities at higher prices and lowers the cost of capital (reducing adverse selection). In addition, it also reduces the tendency of managers to take self-beneficial actions such as "additional consumption," thereby suppressing moral hazard behavior (Healy & Palepu, 2001; Biddle & Hilary, 2006).

H1: Good Financial reporting quality has a positive effect on investment efficiency

2.3 Indonesia Sharia Stock Index (ISSI) as a moderating variable on Good Financial Reporting Quality and Investment Efficiency

The formation of moral behavior is influenced by education on Islamic values and regulations that are able to limit fraudulent practices within the company so that managers who have moral behavior are expected to be able to provide a negative response to earnings management practices (Obid & Demikha, 2011). Alam et al. (2017) suggest using the stock market, which is based on Islamic Sharia principles, to protect investor rights. In Indonesia, shares that are included in the Sharia Securities Register (DES) must go through business and financial screening and comply with the transaction and business activities required by the Fatwa of the Indonesian Ulema Council (Fatwa of the National Sharia Council No: 80/DSN-MUI/III/2011 Concerning the Application of Sharia Principles in the Equity-Type Securities Trading Mechanism in the Stock Exchange Regular Market; Fatwa of the National Sharia Council No: 40/DSN-MUI/X/2003 Concerning the Capital Market and General Guidelines for the Application of Sharia Principles in the Capital Market Sector) and the Financial Services Authority (Copy of Financial Services Authority Regulation Number 35/POJK.04/2017 Concerning Criteria and Issuance of List of Sharia Securities; and Copy of Financial Services Authority Regulation Number 15/POJK.04/2015 Concerning Application of Sharia Principles in the Capital Market).

The results of Ismail et al. (2015)'s research on companies on the Malaysia Stock Exchange show that companies that implement Sharia Compliant have a higher quality of earnings compared to Non-Sharia Compliant. In line with Can (2020), who examined 2300 companies in 15 Muslim-majority countries proving that Sharia compliance and the use of Islamic financial instruments improve the quality of financial reporting through the repeal of discretionary accruals. Hutauruk et al. (2021) compared the performance of companies that have conventional shares and Islamic shares in 2015-2020. He found that companies whose shares are listed in the Sharia Stock Index tend to experience healthier financial conditions and do not experience financial distress. The results of research by Yapono & Khomsatun (2018) prove that lower earnings management increases investment efficiency in a sample of public companies that are included in the Sharia Securities List (DES).

H2: Company status listed on the Indonesia Sharia Stock Index (ISSI) strengthens the positive effect of good financial reporting quality on investment efficiency

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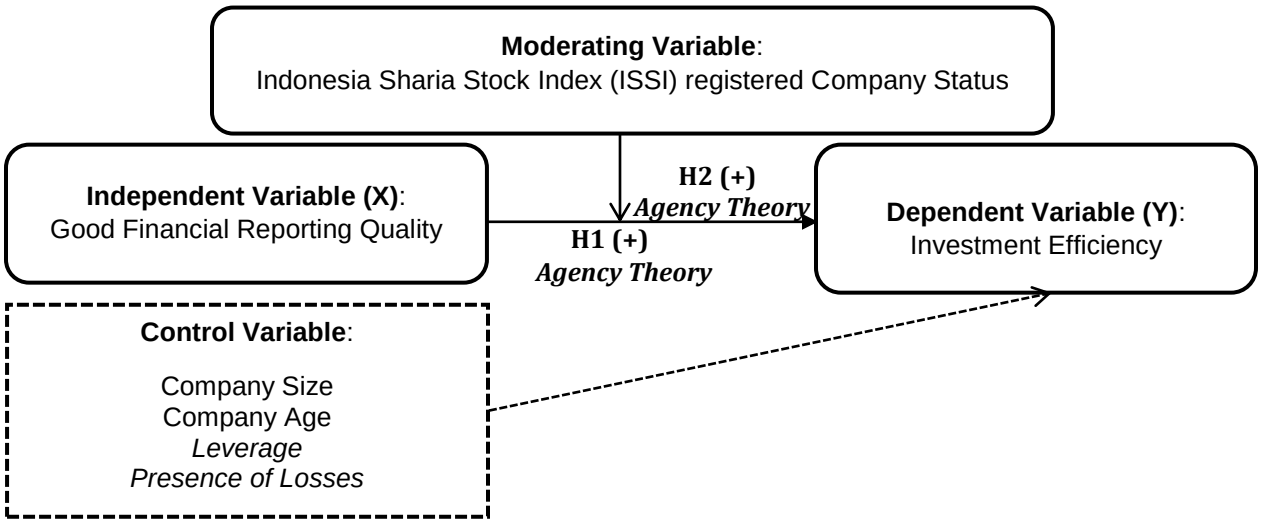

Image1. Conceptual Framework

Source: Processed Data (2023)

3. RESEARCH METHODS

Table 1. Sample Selection Results

No.	Criteria	Total
1	Number of companies listed on the Indonesia Stock Exchange for the 2019-2021 period	530
2	Companies included in the financial sector	(106)
3	Companies listed on the IDX that do not consistently issue audited annual financial reports from 2019 – 2021; and the financial reporting period does not end on December 31;	(28)
4	The financial statements are presented in a currency other than Rupiah	(79)
5	The company does not have the data needed for the research	(65)
	Number of Companies (Sample)	**252**
	Number of Observations = 252 x 3 years (2019-2021)	**756**

Source: Processed Data (2023)

The sample in this study is all sector companies (except financial sector companies) listed on the Indonesia Stock Exchange (IDX) for the 2019-2021 period. Based on the purposive sampling technique, this study obtained 252 samples and 756 firm-year observations.

The data source used is secondary data obtained through the official website of the Indonesia Stock Exchange (IDX); the sample company's official website; as well as other relevant sources. This study used panel data regression statistical analysis and moderated regression analysis (MRA) processed with Econometric Views 13(EViews13) software. The operational definitions of the variables are shown in Table 2 below:

Table 2. Definition of Operational Variables

Variables	Symbol	Explanation
Dependent Variable:		
Investment efficiency	INVEF	The total investment of company *i* in year *t*, namely the sum of capital expenditures plus research and development expenditures, and then deducting sales in fixed assets and divided by the total assets of the previous year. The residual value of the investment model is then absolute and then multiplied by -1 (Chen et al., 2011; Handayani et al., 2016; Siregar & Nuryanah, 2019)
Independent Variable:		
Good Financial Reporting Quality	FRQDAKOT	The absolute value of the residual (discretionary accruals) multiplied by -1 (Kothari et al., 2005) because of the Good financial reporting quality is the opposite of discretionary accruals.
	FRQDAKAS	The absolute value of the residual (discretionary accruals) multiplied by -1 (Kasznik, 1999) because of the good financial reporting quality is the opposite of discretionary accruals.
	FRQDISREV	The absolute value of the residual (discretionary revenue) multiplied by -1 (Mcnichols & Stubben, 2008) because of the good financial reporting quality is the opposite of discretionary revenue.

Moderating Variable:		
Indonesia Sharia Stock Index (ISSI) Registered Company Status	ISSI	*The dummy* score is "1" if the company is registered with ISSI and "0" otherwise (Pratiwi & Siswantoro, 2017)
Control Variable:		
Company Size	CS	Natural logarithm (Ln) of total assets (Shahzad et al., 2019)
Company Age	AGE	Natural logarithm (Ln) of the company's age (Chen et al., 2011; Handayani et al., 2016; Shahzad et al., 2019)
Leverage	LEV	The ratio of total debt to total assets (Shahzad et al., 2019)
Presence of Losses	LOSS	Dummy, score "1" if the company loses, score "0" if the company makes a profit (Biddle et al., 2009; Shahzad et al., 2019)

Source: Processed Data (2023)

4. RESULTS

4.1 Descriptive Statistics

Table 3. Statistic Descriptive Results

	Mean	Maximum	Minimum	Std. Deviation
INVEF	-0.034520	-0.000003	-0.218585	0.034334
FRQDAKOT	-0.053744	-0.000085	-0.275395	0.049517
FRQDAKAS	-0.051126	-0.000077	-0.324256	0.050631
FRQDISREV	-0.029348	-0.000012	-0.352486	0.038173
CS	28.72029	33.53723	18.17144	1.716595
AGE	3.498384	4.919981	1.609438	0.458154
LEV	0.483841	3.954365	0.002672	0.349681

Source: Processed Data (2023)

On average, the investment efficiency made by companies is -0.034520. The maximum INVEF value is -0.000003, and the minimum value is -0.218585. The standard deviation of the INVEF variable has a value of 0.034334. The quality of financial reporting (FRQDAKOT, FRQDAKAS, and FRQDISREV) used in this study is an absolute number from the residual of discretionary accrual regression model because this study does not look at whether there is

an “income increasing” or an “income decreasing”, but looks at the amount of earnings management that occurs. The average value of the FRQDAKOT variable is-0.053744, the maximum value of FRQDAKOT is -0.000085, and the minimum value is -0.275395 with a standard deviation of 0.049517. The average value of the FRQDAKAS variable is -0.051126. The maximum value of FRQDAKAS is -0.000077, and the minimum value is -0.324256 with a standard deviation of 0.050631. The average value of the FRQDISREV variable is -0.029348. The maximum value of FRQDISREV is -0.000012, and the minimum value is -0.352486 with a standard deviation of 0.038173.

The average value of the CS variable is 28.72029. The maximum value of CS is 33.53723, and the minimum value is 18.17144 with a standard deviation of 1.716595. The average value of the AGE variable is 3.498384, with a maximum AGE value of 4.919981 and a minimum value of 1.609438. The AGE standard deviation of 0.458154. The average value of the LEV variable is 0.483841, which means that, on average, the sample companies use relatively high debt to finance their operational and investment activities. The maximum LEV value is 3.954365, and the minimum value is 0.002672, with a standard deviation of 0.34968.

Table 4. Statistic Descriptive *Dummy* Variable

Variable	N	*Dummy* = 1	*Dummy* = 0
ISSI	756	70.2%	29.8%
LOSS	756	32.8%	67.2%

Source: Processed Data (2023)

Table 4 shows that there are more companies listed on the Indonesia Sharia Stock Index (ISSI) than companies that are not listed on the Indonesia Sharia Stock Index (ISSI). This data indicates that the development of Sharia stocks in Indonesia in 2019-2021 is quite high, as seen from the proportion of the number of companies listed on the Indonesia Sharia Stock Index (ISSI) of 70.2%. In addition, it is known that from a total of 756 observations, the proportion of companies that experienced losses from 2019-2021 was 32.8% lower than the proportion of companies that did not suffer losses, with a proportion of 67.2% of the total observations.

4.2 Selection Model Estimation Data Panel (Chow Test, Hausman Test, and LM Test)

Table 5. Panel Data Estimation Model (FRQDAKOT)

Test	Model 1		Model 2	
	Prob.	Decision	Prob.	Decision
Chow	0.0000	FEM	0.0000	FEM
Hausman	0.0110	FEM	0.0154	FEM
LM	0.0038	FEM	0.0061	FEM
		FEM		**FEM**

Description:
CEM: *Common Effect Model*
FEM: *Fixed Effect Model*
REM: *Random Effect Model*

Source: Processed Data (2023)

The selected panel data estimation technique for the FRQDAKOT model with direct testing is the fixed effect model (FEM) because the significance level of α on the Hausman Test is < 0.05 (0.0110). In models that include moderating variables, the selected panel data estimates are random effect models (FEM). This can be seen from the significance level α of the Hausman Test is < 0.05 (0.0154).

Table 6. Panel Data Estimation Model (FRQDAKAS)

Test	Model 1		Model 2	
	Prob.	Decision	Prob.	Decision
Chow	0.0000	FEM	0.0000	FEM
Hausman	0.0090	FEM	0.0146	FEM
LM	0.0053	FEM	0.0071	FEM
		FEM		**FEM**

Description:
CEM: *Common Effect Model*
FEM: *Fixed Effect Model*
REM: *Random Effect Model*

Source: Processed Data (2023)

The selected panel data estimation technique for the FRQDAKAS model with direct testing is the fixed effect model (FEM) because the significance level of α on the Hausman Test is < 0.05 (0.0090). In models that include moderating variables, the selected panel data estimates are common effect models (FEM). This can be seen from the significance level α of the Hausman Test is < 0.05 (0.0146).

Table 7. Panel Data Estimation Model (FRQDISREV)

	Model 1		Model 2	
Test	**Prob.**	**Decision**	**Prob.**	**Decision**
Chow	0.0000	FEM	0.0000	FEM
Hausman	0.0108	FEM	0.0160	FEM
LM	0.0045	FEM	0.0057	FEM
		FEM		**FEM**

Description:
CEM: *Common Effect Model*
FEM: *Fixed Effect Model*
REM: *Random Effect Model*

Source: Processed Data (2023)

The panel data estimation technique chosen for the FRQDISREV model by direct testing is the common effect model (FEM) because the significance level is α on the Hausman Test is < 0.05 (0.0108). In models that include moderating variables, the selected panel data estimates are common effect models (FEM). This can be seen from the significance level α of the Hausman Test is < 0.05 (0.0160).

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4.3 Regression Equation Test

Table 8. Regression Test without Moderating Variable

Variable	FRQDAKOT	FRQDAKAS	FRQDISREV
FRQ	***0.0000 (+)	***0.0004 (+)	*0.0553 (+)
CS	0.1093 (-)	0.0524 (-)	0.0791 (+)
AGE	0.0000 (+)	0.0000 (+)	0.0000 (-)
LEV	0.0124 (-)	0.0058 (-)	0.0002 (+)
LOSS	0.0981 (+)	0.0003 (+)	0.0000 (-)
Adjusted R²	66.4%	68.7%	72.3%
Prob(F-Statistic)	0.0000	0.0000	0.0000
*****;**;*: 1%; 5%; 10% Significance level**			

Source: Processed Data (2023)

Table 9. Regression Test by including Moderating Variable

Variable	FRQDAKOT	FRQDAKAS	FRQDISREV
FRQ	0.5705 (-)	0.5967 (-)	0.5368 (-)
ISSI	0.0000 (+)	0.0004 (+)	0.0003 (+)
FRQ*ISSI	***0.0001 (+)	**0.0395 (+)	***0.0073 (+)
CS	0.0365 (-)	0.0247 (-)	0.0123 (-)
AGE	0.0000 (+)	0.0000 (+)	0.0000 (+)
LEV	0.0041 (-)	0.0099 (-)	0.0012 (-)
LOSS	0.0306 (+)	0.0108 (+)	0.0001 (+)
Adjusted R²	64.3%	65.8%	68.2%
F Statistic	0.0000	0.0000	0.0000
*****;**;*: 1%; 5%; 10% Significance level**			

Source: Processed Data (2023)

Table 8 shows the results of the regression test without moderating variable. Based on the table above, the independent variables, namely the quality of financial reporting and the control variable, are able to explain variations in investment efficiency using FRQDAKOT proxies of 66.4 %, FRQDAKAS of 68.7%, and FRQDISREV of 72.3%. The results of the F test for direct testing show a probability value of 0.000000 in the third proxy with a value of $\alpha < 0.05$, so it is said to be significant. This sign indicates that together the quality of financial reporting and the control variables have a significant influence on investment efficiency. Table 4 shows the regression results from FRQDAKOT has a coefficient of

0.064984 (P value = 0.0000); FRQDAKAS has a coefficient of 0.038436 (P value = 0.0004); FRQDISREV has a coefficient of 0.026966 (P value = 0.0553) indicating a positive effect of good financial reporting quality on investment efficiency at a significance level of α < 1% and < 10%.

Table 9 shows that good financial reporting quality and control variables can explain variations in investment efficiency in the proxies FRQDAKOT (64.3%), FRQDAKAS (65.8%), and FRQDISREV (68.2%). The results of the F test for testing, including the moderating variable, show a probability value of 0.000000 which has a value <0.05, so it is said to be significant. This sign indicates that together the quality of financial reporting, the status of companies listed in the Indonesia Sharia Stock Index (ISSI), and control variables have a significant influence on investment efficiency.

Regression results of the interaction variables using three proxies for the quality of financial reporting, namely FRQDAKOT*ISSI has a coefficient of 0.114473 (P value = 0.0001); FRQDAKAS*ISSI has a coefficient of 0.053309 (P value = 0.0395); FRQDISREV*ISSI has a coefficient of 0.083215 (P value = 0.0073) indicating that the status of companies listed on the Indonesia Sharia Stock Index (ISSI) reinforces the positive influence of good financial reporting quality on investment efficiency at a significance level of α < 1% and < 5%.

5 DISCUSSION

5.1 The Effect of Good Financial Reporting Quality on Investment Efficiency

The results show that good financial reporting quality has a positive effect on investment efficiency in accordance with the first hypothesis and provides empirical evidence against agency theory regarding the importance of good financial reporting quality as a means of reducing information asymmetry between managers (agents) and shareholders (principals) thereby encouraging the creation of efficiency investment. Investments made by the company are trusted capital provided by shareholders. The company must carry out this mandate by placing its funds by making efficient investments (Yapono & Khomsatun, 2018). Financial reporting quality can function as an effective oversight mechanism to suppress problems that arise as a result of information asymmetry between agents and principals due to the support of reliable, transparent, relevant, and comparable financial information that assists investors in making investment decisions.

The results of this study support the research by Biddle et al. (2009), which states that high financial reporting quality can facilitate companies experiencing financial constraints

to obtain additional capital by showing their projects that generate positive net present value (NPV) to investors, thereby reducing opportunities for underinvestment. Managers are also required to be more responsible because there is more optimal supervision of managerial activities, which reduces the opportunity for managers to invest in projects that have a negative net present value (NPV), thereby preventing overinvestment (Handayani et al., 2016).

Financial reports have a positive effect on investment efficiency as measured using the discretionary accrual model of Kothari et al. (2005), the discretionary accrual model of Kasznik (1999), and the Revenue Discretionary Model of McNichols and Stubben (2008). Earnings is an important component that is considered by users of financial statements because earnings information generated by the company shows management achievement as well as an indicator of management performance evaluation (Rachmasari & Darsono, 2015; Sari & Ahmar, 2014). Accrual quality is an indicator to measure the quality of financial statements because accruals are better able to represent future earnings than cash flow basis, which has timing and mismatching problems (Dechow, 1994; Verdi, 2006; and Marlinah, 2015). However, accrual basis is also possible there is self-interested behavior of managers to carry out earnings management to increase or decrease the accrual figures in the income statement (Rachmawati & Triatmoko, 2007).

Therefore, this study uses discretionary accruals and discretionary revenue to determine the extent to which companies manage earnings for the purpose of opportunities. The results of this study are in line with the findings of Biddle et al. (2009); Chen et al. (2011); Handayani et al. (2016); Shahzad et al. (2019); and Ardianto et al. (2021) who support the importance of good financial reporting quality to achieve an efficient level of investment considering that Indonesia's incremental capital output ratio (ICOR) is among the highest in ASEAN in recent years. The actions of handling financial reports carried out by several large companies in Indonesia indicate the need for improvement in regulation to encourage an increase in the quality of financial information, including rules regarding ethics and corporate integrity in complying with applicable accounting standards.

The results of this study are in line with Verdi (2006)'s research; Biddle et al. (2009); Chen et al. (2011); Gomariz & Ballesta (2013); Shahzad et al. (2019); and Ardianto et al. (2021) stated that increasing investment efficiency could occur through improving financial reporting quality. Different results were shown by Umiyati & Riyanto (2019), who stated that there was no effect on financial reporting quality on overinvestment and

underinvestment (Gomariz & Ballesta, 2013) also found that higher financial reporting quality is proven to reduce overinvestment but not proven to reduce underinvestment.

5.2 The Effect of Good Financial Reporting Quality on Investment Efficiency by Using The Status of Companies Listed in The Indonesia Sharia Stock Index (ISSI) as a Moderating Variable

The status of companies listed on the Indonesia Sharia Stock Index (ISSI) strengthens the influence of good financial reporting quality on investment efficiency. The results of this study also support the agency theory which assumes that there is self-interest behavior that underlies unequal desires, motivations, and utilities between management and shareholders, giving rise to the possibility of management behaving unethically by taking actions that are detrimental to shareholders such as reporting earnings opportunistically resulting in low earnings quality (Rachmawati & Triatmoko, 2007). The formation of moral behavior is also influenced by the values of Islamic education (Obid & Demikha, 2011).

The average leverage ratio of companies listed on ISSI is 0.40, much lower than the leverage ratio of non-ISSI companies of 0.67. Shares that will enter the DES (list of Sharia securities) must go through a business screening and financial screening, which aims to select the type of business, business activities, and transactions from companies that comply with Sharia Principles. It is feared that the relatively large proportion of leverage will cause the company to experience financial difficulties, including debt repayment constraints. Creditors will also consider providing loan funds as well as supervision for companies that are indicated to have tight liquidity problems. This worrying condition could affect investors' interest in investing. Lack of "injection" of external funds will disrupt the company's financial condition, which can cause the company to miss the opportunity to invest in projects that have a positive Net Present Value (NPV), resulting in underinvestment conditions.

Contracts in Sharia transactions use *the Profit-Loss Sharing principle* so that if there is a loss in the business, it will be borne by all parties involved in the engagement. Companies whose shares are listed in the Sharia Stock Index tend to experience healthy financial conditions and do not experience financial distress (Hutauruk et al., 2021). The proportion of companies listed on ISSI, as much as 70.2% of a total of 756 observations, has had a significant influence in improving the quality of financial information required by shareholders for making investment decisions. The increase in the realization of national investment in recent years, accompanied by honest types of business and transactions

without any loss, fraud, elements of usury, and other things prohibited in Sharia provisions, is expected to increase investor confidence in companies so that companies can invest in projects that have NPV positive.

The results of this study support the research of Obid & Demikha (2011), which states that from an Islamic perspective, business and management decisions consider the "Accountability of God" in every decision-making in disclosing financial information accurately and correctly. Although not all companies listed on the Indonesia Sharia Stock Index (ISSI) fully comply with Sharia principles, most of them tend to minimize violations of these principles (Pratiwi & Siswantoro, 2017). According to Ismail et al. (2015), companies that implement Sharia compliance have a higher quality of earnings compared to other companies. Companies with Sharia status also have great demands in providing high-quality financial reporting. This is coupled with the existence of fairly tight supervision from policymakers and institutional investors. The same thing was mentioned by Can (2020) that Sharia compliance and the use of Islamic financial instruments have a positive influence on financial reporting quality by reducing discretionary accruals and increasing audit aggressiveness.

6 CONCLUSION

This study aims to empirically examine the effect of good financial reporting quality on investment efficiency, which is moderated by the status of companies listed on the Indonesia Sharia Stock Index (ISSI). The research sample is 252 companies (756 observations). The results showed that good financial reporting quality has a positive effect on investment efficiency. The results of this study provide empirical evidence that the higher quality of financial reporting is able to reduce information asymmetry between managers (agents) and shareholders (principals) due to an increase in the quality of information about company conditions that influence investment decision-making by managers and shareholders. The status of companies listed on the Indonesia Sharia Stock Index (ISSI) is also proven to strengthen the effect of financial reporting quality on investment efficiency.

6.1 Contributions

This research has contributions to theory, practice, and policy. The theoretical contribution of this study can provide benefits to agency theory as the basic theory used to analyze the relationships and conflicts that occur between agents (managers) and principals (investors) through empirical evidence that states that good financial reporting quality has a positive effect on investment efficiency and company status listed in the

Indonesia Sharia Stock Index (ISSI) also strengthens the effect of good financial reporting quality on investment efficiency by reducing information asymmetry. Second, the practical contribution of this research can be an input for companies to improve good financial reporting quality because the importance of the role of good financial reports as a basis for making investment decisions that are more accurate for investors is supported by the existence of provisions governing the prohibition regarding transactions, business activities and certain types of business in accordance with sharia principles which has an impact on reducing information asymmetry. Third, the policy contribution of this research can be used as material for consideration for policymakers in establishing regulations that encourage the improvement of financial reporting quality as well as the basis for forming policies that support the development of the Islamic Capital Market as a driver for the realization of national investment efficiency.

6.2 Limitations of This Study

The limitation of this study is the subjectivity of researchers in understanding and interpreting the information contained in the financial statements as a source of data in this study. In addition, the period for this study is only 3 years, namely 2019-2021. Future studies may use a longer period. Furthermore, this study only uses one Islamic stock index as a moderating variable. It is hoped that further research can add other Islamic stocks, such as the Jakarta Islamic Index (JII) and the Jakarta Islamic Index 70 (JII70), as moderating variables. Third, the results of this study only use three proxies for financial reporting quality. Future research can use other proxies such as working capital accruals (Chen et al., 2011; Gomariz & Ballesta, 2013), readability of financial statements (Biddle et al., 2009), and value relevance of accounting information. Fourth, this study only uses one investment efficiency proxy. Future research can use other measurements such as fixed asset growth (Mcnichols & Stubben, 2008); using investment cash flow sensitivity (Biddle & Hilary, 2006), as well as separating overinvestment and underinvestment conditions based on cash balances and company leverage (Biddle et al., 2009).

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