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Determinants of Share Price: A Case of Automobile Industry in Malaysia

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Abstract:

This research investigates the determinants of share price in the Malaysian automobile industry by using financial ratios such as book value per share, earnings per share, price-earnings ratio and return on equity within the time span of year 2001 to 2015 using the quarterly data sourced from Wall Street Journal and sample companies' quarterly reports. Augmented Dickey-Fuller and Phillips-Perron unit root test are used to test the stationarity of data and the variables are found to be stationary at first difference. Data were analyzed with regression models to reveal the linkage between the explanatory variables and share price. Results revealed that the EPS and P/E ratio are significantly and positively correlated to share price. Book value per share is also positively correlated to the share price but the strength of the relationship is unidentified. However, the relationship of return on equity and share price is undecided due to contradicting results.

Keywords:Share Price, Book Value per Share, Earnings per Share, Price-Earnings Ratio, Return on Equity

I. INTRODUCTION

In the early 1980s, the Heavy Industrial Policy was introduced by Malaysia's then prime minister, Tun Dato' Seri Dr Mahathir bin Mohamad, and it has led to significant changes onto the Malaysian industrialisation strategy and ultimately building Malaysia's nationally owned automotive project, Proton. Subsequent to Malaysia's first National Car Project in year 1983, protective measures like the tariff and non-tariff barriers, as well as local content policy was adopted by the Malaysian government, in hope that these measures will help the Malaysian automobile industry to develop and expand locally. This shows Malaysian government's effort in protecting the industry and the economic prosperity. The automobile industry in Malaysia has been growing tremendously from year 1980 to 2010 and with the Malaysian National Automotive Policy (NAP) launched in 2014, the automobile industry is set to growth stronger in the following years and it is forecasted that this industry will contribute to 10% of Malaysia's gross domestic product by 2020.

Strong growth in companies will facilitate strong growth in a country's economy, however in order for a company to grow, resources are needed. Stock markets can help to ensure that there is a flow of resources to the productive investment opportunities. When a company shows good performance, there will be a heightened demand for that share, thus boosting the share price and vice versa. Performance of companies can be measured by using financial ratios; therefore this study aims to uncover the determinants of share price by using financial ratios.

II. PROBLEM STATEMENT

The stock market is a platform where it allows the investors to do trading and investors can possibly gain extra earnings through their trading activities. By understanding determinants of share price for companies operating in the Malaysian automobile industry, investors will most definitely be able to reap the benefits from the possible growth in the Malaysian automobile industry as they can identify a potential investment opportunity in the market earlier than any average person.

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As mentioned in the earlier parts of this documentation, the Malaysian government is highly protective towards the automobile industry. The action has proven that the automobile industry is seen as an important industry for Malaysia; therefore it has also influenced the desire to conduct this research on the automobile industry.

Attributed to the fact that the equity market plays a crucial role in facilitating the economic activity, many of the researchers have studied the determinants of share price, especially for developed countries. The studies usually involve developed countries' share market as a whole or a certain industry in the developed countries. However in emerging countries like Malaysia, fewer studies concerning this issue have been conducted. In the Malaysian context, a similar study has been conducted and the research was solely focused on the property sector of Malaysia only (Chan et al., 2012), thus far, there are no similar research addressing the automobile industry of Malaysia has been conducted.

Considering that the automobile industry in Malaysia might experience strong growth in the following years and no research of the same topic has been conducted to address the Malaysian automobile industry, therefore this research seeks to uncover the determinants of share price fluctuations for companies operating within the automobile industry in Malaysia.

III. LITERATURE REVIEW

The determinants of share price have been widely studied by many researchers (Khan et al, 2012; Malhotra & Tandon, 2013; Wang et al, 2013; Menike & Prabath, 2014; Arshad et al, 2015). Sharma (2011) studied the relationship between accounting variables and share price in the Indian context by using explanatory variables such as book value per share, dividend per share, dividend yield and price-earnings ratio. Results revealed that dividend per share, book value per share and earnings per share can significantly influence share price. Wang et al (2013) studied the relationship between accounting information and the stock returns in the Shanghai Stock Exchange, results showed that earnings per share and return on equity has the strongest impact on share price and the researchers then concluded that accounting information is a determinant of share price.

Khan et al's (2012) research also found that dividend yield, earnings yield and book value per share are directly and positively associated with the share prices and book value per share has the highest predictive among all. Menike and Prabath (2014) also investigated the impact of accounting variables on stock prices in Colombo Stock Exchange from year 2008 to year 2012 and the results showed that book value per share, earnings per share and dividend per share all have significant impact on stock prices.

Using the multiple linear regression model, Arshad et al's (2015) study has attempted to study the relationship between dividend per share, book to market ratio, earnings per share and price-earnings ratio with share price of commercial banks listed on the Karachi Stock Exchange. Findings revealed that theearnings per share can strongly influence share price, whereas book to market value is negatively correlate to share price, and dividend per share and price-earnings ratio are found to have no relationship with share price volatility.

IV. METHODOLOGY

This research focuses on the Malaysian automobile industry by selecting 5 listed companies that are involved in the Malaysian automobile industry, including Cycle and Carriage Bintang Berhad, DRB Hi-Com Berhad, Sime Darby Berhad, Tan Chong Motor Holdings Berhad and UMW Holdings Berhad. The explanatory variables used in this study are book value per share, earnings per share, price-earnings ratio and return on equity. Data were obtained from the sample companies' quarterly reports and Wall Street Journal, on a quarterly basis for the period covering year 2001 to year 2015.

The brief description of each explanatory variable used is presented below.

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Book Value per Share:

The book value per share measures the amount of assets in respect to each unit of share. Higher book value usually means that the particular company has got good and healthy past organizational performance such as large amount of reserves. Formula is as below:

$$Book\ Value\ per\ Share = \frac{Equity\ Share\ Capital}{Total\ Number\ of\ Equity\ Shares\ Outstanding}$$

Earnings per Share:

Earnings per share give a very straightforward measure on how the earnings of the company are being distributed across the number of outstanding shares. This ratio appears to be one of the most commonly used ratios used by financial analysts due to its practicality (Turk & Chapman, 2006). This ratio is arrived as below:

$$Earnings\ Per\ Share = \frac{Net\ Profits\ After\ Tax - Preference\ Dividend}{Number\ of\ Equity\ Shares\ Outstanding}$$

Price-Earnings Ratio:

The ratio is a common measure to the value of the shares as it gives investors an insight of the price of shares against the earning power of the share itself. Investors also view the price earnings ratio to estimate the future earning power of the firms where firms with high price earnings ratio will be seen to have high growth opportunities.

$$Price\ Earnings\ Ratio = \frac{Price\ per\ Share}{Earnings\ per\ Share}$$

Return on Equity:

Return on equity measures how much profit a firm can generate with every one dollar of shareholders' equity and it also can communicate to shareholders on how effective is the company in employing the money they have invested. The higher the return of equity signifies the better the management is utilizing shareholders' money to generate profit.

$$Return\ on\ Equity = \frac{Net\ Income}{Total\ Shareholders'Equity}$$

V. FINDINGS

Logarithmic transformation was applied to the data because when the raw data was tested for unit root, the data was found to not be stationary even at second difference. By applying logarithmic transformation, high value variables can be compressed to low value variables by using order of magnitude to express the order. Logarithmic transformation can also make data more normally distributed. After applying logarithmic transformation, several tests are conducted to investigate the linkages the financial ratios and share price, including unit root test and multiple linear regression.

VI. UNIT ROOT TEST

It is important to conduct unit root test to assess the stationarity of data at early stage as to avoid false regression that will reject true relationship accept false relationship when non-stationary data are used for analysis. Unit root tests adopted in this research are the Augmented Dickey-Fuller (ADF) test and Phillips-Perron (PP) test. The results of the stationarity test based on Augmented Dickey-Fuller and Phillips-Perron are shown in Table 2 below.

TABLE 1:
ADF Test Results for Cycle and Carriage Bintang Berhad

	Augmented Dickey Fuller											
	Intercept (Prob – Lag Length)						**Trend (Prob – Lag Length)**					
	Level		**1st Difference**		**2nd Difference**		**Level**		**1st Difference**		**2nd Difference**	
LBVPS	0.4827	0	0.0000	0	0.0000	2	0.8483	0	0.0000	0	0.0000	2
LEPS	0.0771	4	0.0089	3	0.0000	2	0.2769	4	0.0281	3	0.0000	2

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LPE	0.0343	4	0.0062	3	0.0000	2	0.1018	4	0.0243	3	0.0000	2
LROE	0.0773	4	0.0056	3	0.0000	2	0.2840	4	0.0227	3	0.0000	2
LSP	0.3213	0	0.0000	0	0.0000	1	0.7379	0	0.0000	0	0.0000	1

TABLE 2:
PP Test Results for Cycle and Carriage Bintang Berhad

	Phillips-Perron					
	Intercept (Prob)			**Trend (Prob)**		
	Level	**1st Difference**	**2nd Difference**	**Level**	**1st Difference**	**2nd Difference**
LBVPS	0.5092	0.0000	0.0001	0.8870	0.0000	0.0001
LEPS	0.0003	0.0000	0.0001	0.0004	0.0000	0.0001
LPE	0.0000	0.0000	0.0001	0.0001	0.0000	0.0001
LROE	0.0000	0.0000	0.0001	0.0002	0.0000	0.0001
LSP	0.2516	0.0000	0.0001	0.6206	0.0000	0.0001

TABLE 3:
ADF Test Results for DRB Hi-Com Berhad

	Augmented Dickey Fuller											
	Intercept (Prob – Lag Length)						**Trend (Prob – Lag Length)**					
	Level		**1st Difference**		**2nd Difference**		**Level**		**1st Difference**		**2nd Difference**	
LBVPS	0.2892	0	0.0000	0	0.0000	0	0.6014	0	0.0000	0	0.0000	0
LEPS	0.0073	0	0.0000	0	0.0000	2	0.0520	0	0.0000	0	0.0000	2
LPE	0.0000	1	0.0000	2	0.0000	2	0.0000	1	0.0000	1	0.0000	2
LROE	0.0086	0	0.0000	2	0.0000	2	0.0562	0	0.0000	2	0.0000	2
LSP	0.1920	0	0.0000	0	0.0000	1	0.5701	0	0.0000	0	0.0000	1

TABLE 4:
PP Test Results for DRB Hi-Com Berhad

	Phillips-Perron					
	Intercept (Prob)			**Trend (Prob)**		
	Level	**1st Difference**	**2nd Difference**	**Level**	**1st Difference**	**2nd Difference**
LBVPS	0.2892	0.0000	0.0001	0.6014	0.0000	0.0001
LEPS	0.0082	0.0000	0.0001	0.0593	0.0000	0.0001
LPE	0.0000	0.0000	0.0001	0.0002	0.0000	0.0001
LROE	0.0114	0.0000	0.0001	0.0747	0.0001	0.0001
LSP	0.1654	0.0000	0.0001	0.5211	0.0000	0.0001

TABLE 5:
ADF Test Results for Sime Darby Berhad

	Augmented Dickey Fuller											
	Intercept (Prob – Lag Length)						**Trend (Prob – Lag Length)**					
	Level		**1st Difference**		**2nd Difference**		**Level**		**1st Difference**		**2nd Difference**	
LBVPS	0.0000	0	0.0000	3	0.0000	5	0.0000	0	0.0000	3	0.0000	5
LEPS	0.0160	3	0.0001	2	0.0000	6	0.0524	3	0.0001	2	0.0000	6
LPE	0.0161	3	0.0001	2	0.0000	6	0.0645	3	0.0001	2	0.0000	6
LROE	0.0048	3	0.0001	2	0.0000	6	0.0185	3	0.0001	2	0.0000	6
LSP	0.0000	0	0.0000	0	0.0000	1	0.0001	0	0.0000	0	0.0000	1

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TABLE 6:
PP Test Results for Sime Darby Berhad

	Phillips-Perron					
	Intercept (Prob)			**Trend (Prob)**		
	Level	**1st Difference**	**2nd Difference**	**Level**	**1st Difference**	**2nd Difference**
LBVPS	0.0000	0.0000	0.0000	0.0000	0.0000	0.0000
LEPS	0.0160	0.0001	0.0000	0.0524	0.0001	0.0000
LPE	0.0161	0.0001	0.0000	0.0645	0.0001	0.0000
LROE	0.0048	0.0001	0.0000	0.0185	0.0001	0.0000
LSP	0.0000	0.0000	0.0000	0.0001	0.0000	0.0000

TABLE 7:
ADF Test Results for Tan Chong Motor Holdings Berhad

	Augmented Dickey Fuller											
	Intercept (Prob – Lag Length)						**Trend (Prob – Lag Length)**					
	Level		**1st Difference**		**2nd Difference**		**Level**		**1st Difference**		**2nd Difference**	
LBVPS	0.8743	0	0.0000	0	0.0000	1	0.5790	0	0.0000	0	0.0000	1
LEPS	0.3110	8	0.1855	7	0.0000	10	0.7573	8	0.3567	7	0.0000	10
LPE	0.7072	8	0.0627	7	0.0000	10	0.2628	8	0.1929	7	0.0003	10
LROE	0.6536	8	0.1140	8	0.0000	10	0.8883	8	0.2032	8	0.0000	10
LSP	0.6186	0	0.0000	0	0.0000	0	0.9132	0	0.0000	0	0.0000	0

TABLE 8:
PP Test Results for Tan Chong Motor Holdings Berhad

	Phillips-Perron					
	Intercept (Prob)			**Trend (Prob)**		
	Level	**1st Difference**	**2nd Difference**	**Level**	**1st Difference**	**2nd Difference**
LBVPS	0.8687	0.0000	0.0001	0.4498	0.0000	0.0001
LEPS	0.0000	0.0000	0.0001	0.0000	0.0000	0.0001
LPE	0.0000	0.0001	0.0001	0.0000	0.0001	0.0001
LROE	0.0000	0.0000	0.0001	0.0000	0.0000	0.0001
LSP	0.5292	0.0000	0.0000	0.7123	0.0000	0.0000

TABLE 9:
ADF Test Results for UMW Holdings Berhad

	Augmented Dickey Fuller											
	Intercept (Prob – Lag Length)						**Trend (Prob – Lag Length)**					
	Level		**1st Difference**		**2nd Difference**		**Level**		**1st Difference**		**2nd Difference**	
LBVPS	0.9138	0	0.0000	0	0.0000	1	0.4545	0	0.0000	0	0.0000	2
LEPS	0.5560	4	0.9816	3	0.0000	2	0.9917	4	0.9977	3	0.0000	2
LPE	0.8724	4	0.7148	3	0.0000	2	0.9499	4	0.9110	3	0.0000	2

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LROE	0.9817	8	0.9997	7	0.1580	6	1.0000	8	0.9999	6	0.3470	6
LSP	0.3419	0	0.0000	0	0.0000	0	0.4523	1	0.0000	0	00000	0

TABLE 10:
PP Test Results for UMW Holdings Berhad

	Phillips-Perron					
	Intercept (Prob)			**Trend (Prob)**		
	Level	**1st Difference**	**2nd Difference**	**Level**	**1st Difference**	**2nd Difference**
LBVPS	0.9138	0.0000	0.0001	0.4716	0.0000	0.0001
LEPS	0.0029	0.0000	0.0000	0.0173	0.0000	0.0000
LPE	0.0003	0.0000	0.0000	0.0006	0.0000	0.0000
LROE	0.0009	0.0000	0.0000	0.0125	0.0000	0.0000
LSP	0.3678	0.0000	0.0000	0.5807	0.0000	0.0000

Based on the results presented above, it is concluded that the variables are only stationary at first difference and therefore, the regression models are reformed, by transforming all the variables into first difference.

Multiple Linear Regression

The multiple linear regression was selected to study the combined effects of the independent variables on the share price. The reformed linear regression models are as follow:

$SP = \alpha + \beta_1 ROE + \beta_2 EPS + \beta_3 BVPS + \beta_4 PE + \varepsilon$

Where,

SP refers to share price,

ROE refers to return on equity,

EPS refers to earnings per share,

BVPS refers to book value per share,

PE refers to price-earnings ratio,

β_n refers to the coefficients of the explanatory variable,

α refers to the estimated constant, and

ε refers to the error term.

To test the compliance of the assumptions of multiple linear regression, several tests have to be conducted and the tests are detailed below.

Multicollinearity Test:

Multicollinearity test is conducted to determine whether the independent variables are correlated. Under a good regression model, correlation between the independent variables should be absent. This test is conducted by assessing the value inflation factor (VIF) and tolerance (TOL).

In this research, it was found that 4 out of 5 of the regression models have multicollinearity, except the regression model of Cycle and Carriage Bintang Berhad. The high multicollinearity problem among variables can be explained by the components of the financial ratios as the financial ratios that are found to have high collinearity with one another, including EPS, ROE and PE, are computed by using the same financial information.

Return on equity is computed by dividing net profit by total equity, whereas earnings per share is computed by dividing net profit to the number of outstanding shares. Therefore when the net profit grows, the value for both the ratio would also increase, ultimately leading to high correlation between these two independent variables. On the other hand, the price-earnings ratio is calculated by dividing price per share with earnings per share; therefore, naturally these two independent variables will have high correlation. However, according to Paul (2006), multicollinearity will not pose a problem and produce false predictions if the R^2 can gauge how well can the model that predict the value of Y.

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Heteroscedasticity Test:

Heteroscedasticity is an assumption to test the variance of residual across all levels of the independent variables. A regression model is deemed to be free from heteroscedasticity if no specific patterns are formed on the charts.

TABLE 11:
Heteroscedasticity Test Results Summary

Company	P-Value of F-Statistics
Cycle and Carriage Bintang Berhad	0.2007
DRB Hi-Com Berhad	0.4493
Sime Darby Holdings Berhad	0.2933
Tan Chong Motor Holdings Berhad	0.7001
UMW Holdings Berhad	0.3813

The heteroscedasticity test results summarized in Table 11 shows that all the five companies' regression models do not have a heteroscedasticity problem as it has all exceed the significance level of 0.05. In other words, it also means that the error terms, which refers to the disturbances in the correlation between the independent variables and dependent variables, is the same across all the independent variables.

Autocorrelation:

Autocorrelation refers to the correlation between the sample data that is organized according to data of a certain time series. This test is used to test the correlation between a regression model's errors.

TABLE 12:
Autocorrelation Test Results Summary

Company	P-Value of Chi-Square
Cycle and Carriage Bintang Berhad	0.0984
DRB Hi-Com Berhad	0.0749
Sime Darby Holdings Berhad	0.0909
Tan Chong Motor Holdings Berhad	0.1165
UMW Holdings Berhad	0.0735

Autocorrelation persists when correlation is found between observations. Observing the information above, the results showed that all five regression models of the sample companies do not have autocorrelation problem as the p-value of chi-square have all exceeded the significance level of 0.05.

Model Specification:

Model specification test is conducted to determine whether the regression models are correctly specified and whether the non-linear combinations of explanatory variables can explain the dependent variables.

In this research, the Ramsey RESET test is conducted to test the model specification problem.

TABLE 12:
Autocorrelation Test Results Summary

Company	P-Value of F-Statistics
Cycle and Carriage Bintang Berhad	0.9052
DRB Hi-Com Berhad	0.3072
Sime Darby Holdings Berhad	0.5127
Tan Chong Motor Holdings Berhad	0.6005
UMW Holdings Berhad	0.2814

Results presented above shows that all five regression model of the sample companies do not have any model specification problem. When the regression model does not have any model specification problem, it also indicates that the model is well specified, where the explanatory variables are sufficient to explain the response variable and no important variables have been omitted from the regression model.

Normality Test:

Normality test is conducted to identify whether a data set is normally distributed or not. Histogram of the residual can assist researchers to test the normality's assumption of error terms.

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TABLE 14:
Normality Test Results Summary

Company	P-Value
Cycle and Carriage Bintang Berhad	0.0000
DRB Hi-Com Berhad	0.0001
Sime Darby Holdings Berhad	0.4013
Tan Chong Motor Holdings Berhad	0.1337
UMW Holdings Berhad	0.0000

Findings presented in Table 5.2.3.1 revealed that 3 out of 5 regression models have a normality problem, including the regression model of Cycle and Carriage Bintang Berhad, DRB Hi-Com Berhad and UMW Holdings Berhad. Put differently, it also means that the error terms in these three aforementioned companies are not normally distributed. According to Ghasemi & Zahediasl (2012), for normality tests, usually it is hard for small sample sizes to reject the null hypothesis. When the sample size of the data is small, the normality distribution of error terms is most likely to be biased (Donald & Lang, 2007).

TABLE 15:
Summary of Regression Model Results

Companies	Independent Variables	Regression Coefficient	P-Value
Cycle and Carriage Bintang Berhad	BVPS	0.4920	0.0000
	EPS	0.9999	0.0000
	PE	0.5080	0.0000
	ROE	0.4920	0.0000
DRB Hi-Com Berhad	BVPS	-2.9415	0.0314
	EPS	4.03E-0.5	0.9924
	PE	0.7950	0.0325
	ROE	0.2734	0.0342
Sime Darby Berhad	BVPS	0.7270	0.6770
	EPS	0.2013	0.0001
	PE	0.8514	0.0144
	ROE	0.0272	0.8861
Tan Chong Motor Holdings Berhad	BVPS	0.0324	0.2160
	EPS	0.9999	0.0000
	PE	0.9676	0.0000
	ROE	0.0325	0.2153
UMW Holdings Berhad	BVPS	-0.3196	0.0000
	EPS	0.9999	0.0000
	PE	1.3196	0.0000
	ROE	-0.3195	0.0000

Regression coefficients show the direction of the relationship between the explanatory variable and share price whereas the p-value reflects whether the independent variable has a significant influence on the share price. When the coefficient value is negative, it signifies that the relationship between the independent variable and share price is negative. The explanatory variable is deemed to have a strong relationship with share price when the p-value is smaller than 0.05.

The results presented in Table 15 shows that 4 out of 5 of the regression model found a positive relationship between book value per share and fluctuation of share price of automobile companies in Malaysia; however the strength of the relationship is unidentified because the p-value for the regression model of Sime Darby Berhad and Tan Chong Motor Holdings Berhad is 0.6770 and 0.2160 respectively, which signifies that the relationship is weak, whereas Cycle and Carriage Bintang Berhad and DRB-Hi-Com Berhad's regression model both have a p-value of 0.000 and 0.0314 respectively, which shows that the relationship is strong.

Results exhibited in Table 15 showed that the relationship between earnings per share and share price is positive and strong as the coefficient values are all positive and the p-value is smaller than 0.05. Similarly for price-earnings ratio, the results also concluded that it is significantly and positively correlated to share price of Malaysian automobile companies.

Based on results presented in Table 15, 3 out of 5 of the regression results showed that the return on equity is positively correlated to share price. Among the 3 regression models, two of which was discovered that the relationship between the financial ratio and share price is weak. However, the remaining two regression models of DRB Hi-Com Berhad and UMW Holdings Berhad have shown that relationship between return on equity and share price is negatively correlated and the strength of

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relationship is weak. The relationship between return on equity and share price is inconclusive due to the conflicting results.

VII. CONCLUSION

This research has investigated the determinants of share prices of Malaysian automobile companies by using financial ratios such as book value per share, earnings per share, price-earnings ratio and return on equity by using the multiple linear regression model. The results obtained have concluded that the book value per share is positively correlated to the share price but the strength of the relationship was not identified, whereas the earnings per-share and price-earnings ratio are revealed to be significantly and positively correlated to the share price. As for return on equity, the relationship between this financial ratio and the share price is unidentified due to the contradicting results that were obtained from this study. The findings of this study support the results from past literature conducted by Sharma (2011), Almumani's (2014), Menike & Prabath (2014), Arshad et al (2015) and Sharif et al. (2015).

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