CHAPTER I
INTRODUCTION

1.1 Background

Given that the global financial system has grown more integrated and less stable, regulators and investors have become increasingly engaged in determining the causes of Stock Price Crash Risk (SPCR) (Srivastava et al., 2024). SPCR is the risk that stock prices will collapse quickly and unexpectedly that affect the value of company and may additionally trigger systemic instability, especially in emerging nations where investor protection and disclosure quality are still uneven (Zonon et al., 2025). SPCR is primarily triggered by knowledge asymmetry and managers exploiting advantage of situations. These problems are made worse by inadequate systems of governance and agency risks, which cause problems between managers and shareholders.

When management suppress bad news or do actions that are good for them, this raises the chance of a SPCR even higher, and also make the company as a whole less stable (Mehri et al., 2025). Thus, researching through the things that cause or lessen SPCR is important for both furthering theoritical progress and making capital markets safer. Investors and regulators in both developed and emerging countries are intrigued in SPCR (Dang & Nguyen, 2021). Due to portfolio diversification does not always reduce idiosyncratic crash risk and for the reason regulators can improve stock market stability, it is important to analyze this risk in emerging markets. Individual stock return distribution with negative skewness is frequently utilized to conceptualize crash risk.

As stated by Hunjra et al. (2020), investors may embrace equities with more negative skewness, or risk of extremely negative returns, in hopes of earning better returns. It is crucial for risk management and invesment decisions to comprehend previous waves of firm-spesific crash risk. Previous research conveys managers' bad news hoarding behavior. According to Lin & Myers' (2006) agency perspective, managers take into account information asymmetries to conceal unfavorable news

for objectives such as career concers, remuneration, or avoiding legal action. This hidden negative information accumulates until it hits a tipping point, after which it is issued all at once, triggering a SPCR (Srivastava et al., 2024). It is challenging for managers to predict when a point is attained and to stop the crash since the highest quantity of unfortunate situations that leaders can conceal varies unpredictably and continually with the firm's changing environment (He & Ren, 2023).

Actual corporate failures show that persistently withholding negative news, alongside deficient governance, eventually risks triggering a severe collapse in stock prices. Bed Bath & Beyond (BBBY) faced a major decline in stock price related to a nexus of strategic mistakes and problems in corporate governance. A bad decision by the board of directors, who quickly approved a $1 billion expedited stock repurchase plan that had to be finished by the end of 2021 (Bed Bath & Beyond Inc., 2021). This option to allocate capital was unwise because it happened when the company's fundamentals were getting worse. Reports say that the firm had bought back $11.8 billion worth of shares since 2004, which depleted reserves of cash that were needed for operations (Isidore, 2023).

The executive team under the company received a significant setback to its integrity when the chief financial officer (CFO) became entangled in shareholder lawsuits as early as August 2022 due to allegations of securities fraud and market manipulation. To be more exact, the CFO offloaded 55,000 shares immediately after the stock reached its peak, just before it began falling at a rapid rate. This action provoked acute speculation of insider trading and artificially pumping up the company stock value, and within several days, the price dropped from approximately $23 USD to $11 USD (Ivanova, 2022). All these governance issues accumulated and led to a massive liquidity crisis which ultimately led Bed Bath & Beyond Inc. to soon declare bankruptcy on April 23, 2023. In the end, this bankruptcy implied the sale of the assets and the eradication of all the values among the public shareholders (Reuters, 2023).

Another example from Indonesia involves the controversy over PT Sri Rejeki Isman Tbk (SRIL), a major player in the textile industry. The Indonesia Stock Exchange has stopped trading this company's shares ever since May 2021, and the firm has officially declared bankruptcy. The director of PT Laba Forexindo Berjangka said that before the suspension, SRIL's stock price had already dropped to IDR 50 per share right after it was taken off the blue-chip stock list (CNN Indonesia, 2025). This huge case was caused by extreme financial constraint due to a bad capital structure. SRIL went bankrupt because abuse of power which leads to a corruption in the credit granting process, along with an aggressive expansion financed by large amounts of debt through extensive global bond issuance (Setiawati, 2025), and caused its share price to fall by around 11% in a week and 24% in a month after the bed news reached the public (Lavinda & Aldin, 2021). The SRIL case highlights the absence of good governance control on financial decisions may turn financial restrictions into permanent market value degradation.

Taken together, these incidents suggest evident trends that are in line with the bad-news hoarding behavior, continued concealment of bad news, poor monitoring, and malfunctioning governance mechanism, which ultimately contribute to a rapid and severe stock price collapses. These practical examples indicate the working practice of SPCR and the importance of good corporate governance in avoidance of such effects. Jin and Myers (2006) declare that managers in secretive or high-risk companies could prioritize their own interests by concealing unfavorable facts, favoring immediate stock effectiveness over the long run worth of the firm. Managers sometimes pursue short-term price maximization strategies, which heighten information asymmetry and increase the future SPCR when adverse information surfaces (Zulfiqar et al., 2022).

Maintaining market confidence while lowering the SPCR depend heavily on effective company governance. Extreme stock fluctuations are less likely when there exists an excellent framework for governance in operation because it boots investor confidence, guarantees managerial accountability, and improves the dependability of corporate decision making. Corporate governance is a framework

of relationships among the management of a business, its directors, stockholders, and other interested parties, backed by systems that set corporate goals, direct their accomplishment and track success (OECD, 2023). According to the National Committee on Governance Policy (KNKG, 2021), it is clear that good corporate governance is not just about the fulfillment of the administrative mandate, but one of the pillars of addressing business risks and long term sustainability.

Most cases of corporate failures are caused by failure of the governing structure to offer effective checks and balances, be it through dubious financial transactions or simply a lack of good strategic decisions. This implies that a robust governance framework is essential to maintain the company on track, adaptable to changes in the market, and contribute to the improvement in value over the period of time. Such an arrangement encourages the most efficient use of resources and provides the members of the board with the appropriate incentives to focus on the needs of the shareholders (Al-Ibbini & Shaban, 2021). It is reinforced by empirical indicators that the inefficient governance mechanism particularly in the developing economy is likely to lead to the elevated SPCR as it is more susceptible to executive interference and insufficient monitoring (Hunjra et al., 2020). Conversely, firms that have stricter governance structures have well-established internal control and their financial reporting is most reliable. This approach lowers information gap between company insiders and outsiders, which in turn build stronger trust in market, making operations more open and clear.

Key features of corporate governance that serve as main monitoring tools include board composition, ownership structure, and audit quality (Zulfiqar et al., 2022). Such mechanisms rest on the foundation of Agency Theory that was created by Jensen and Meckling (1976) and is concerned with a conflict of interest between shareholders (principals) and managers (agents). In this context, board independence is a particular tool to provide objective control through the involvement of unbiased directors (Lawrence et al., 2025), whereas institutional ownership is the existence of advanced investors with the resources and motivation to carefully control the management (Wu et al., 2020). Moreover, audit quality is

used to enhance information asymmetry by proving that there is high quality of auditing (Zulfiqar et al., 2022). The combination of these tools acts to ensure that managerial acts are consistent with shareholder interests and does not lead to bad news hoarding.

This research examines a crucial element of board structure, spesifically board independence. One important governance tool that promotes accountability, transparency, and lessening of information asymmetry in financial markets is board independence, because it boosts monitoring quality and may modify a company's cost of capital, investors frequently see a highly independent board as a favorable indication when making invesment decisions. Independent directors operate as the representative of the shareholders and are expected to be very vigilant in the managerial decision making to preserve investor safety. These directors are supposed to make unbiased decisions and lessen the chances of managerial opportunism. As a result, in order to improve monitoring efficacy and shield shareholders from self-serving managerial behavior, regulators frequently support a larger percentage of independent directors (Doku et al., 2023)

Since independent board members are more capable of providing unbiased supervision and keep an eye on managerial behavior, board independence is essential to improving governance effectiveness. Independent directors can actually reduce the chances of large declines in share price, especially in companies that are subject to highly restrictive regulations. According to a study that supports this viewpoint, companies with independent board leadership have far reduced SPCR, especially those with rigorous oversight requirements (Lawrence et al., 2025).

Institutional ownership is also a crucial procedure of corporate governance that is consistent with the ownership concentration that have been discussed before. Because they own a lot of capital shares, institutions possess strong reasons to monitor how managers act and protect corporate value (Wu et al., 2020). SPCR is a big deal due to institutional stockholders own a lot of assets, when the market goes down, it's hard and expensive to sell them. Real world exposure to tail risks, those rare but devastating market downturns, is gaining more attention from

institutional investors. A global survey by Allianz revealed that more than two-thirds of institutional investors now view extreme downside risks as an emerging worry, which means they are more sensitive to SPCR. On top of that, institutional investors have a history of stepping up with lawsuits, like those stock-drip cases, to show they're alert of SPCR (Chen et al., 2024).

The institutional ownership can play a significant role in reducing the SPCR due to their comprehensive knowledge, superiority in accessing important information, and higher motivation of keeping an eye on monitoring incentives as opposed to ordinary investors. They can evaluate the reports of companies, promote transparency, and prevent the ability of executives to hide the bad news (Farooq et al., 2022). The institutional investor reduces the information asymmetry and discourage executives to stockpile bad news or use any other opportunistic strategies that can result in SPCR, all through requiring prompt and honest disclosure. Chen et al. (2024) discovered a strong indication that the tendency of SCPR is strongly connected with elevated levels of institutional ownership. Their results actually underscore the importance of such big investors being around because they not only have better access to informational advantage but also have the desire to ensure that things are effectively managed to bring a lid to the habit of concealing unfavorable corporate news thus protecting the firms against such disastrous market shocks.

High audit quality is equally critical to handle in the context of corporate governance, which inhibits management's opportunistic conduct and increases the reliability of financial disclosures. The capacity of external auditors in assessing a firm's financial accounts objectively for the own good of stakeholders and the interest of general public is known as audit quality. Higher audit quality lessens disparity of information between executives and shareholders by carefully examining accounting procedures and open disclosure, which eventually lowers the SPCR by reducing the possibility that unfavorable information might be buried (Sultana et al., 2022).

The discoveries of Srivastava et al. (2024), that did a thorough bibliographic and systematic analysis of 485 identified by scopus articles using citation analysis, term combination, bibliographical association, and publishing trend analysis to deepen understanding of crash risk literature, further support the research motivation for examining audit quality in this study. Their analysis shows that audit quality and audit committee effectiveness are two areas that need additional empirical research. It also shows how important corporate governance practices are for lowering SPCR. This analysis incorporates audit quality as a corporate governance variable to evaluate its influence on the occurrence of SPCR, as done by Zulfiqar et al. (2022).

Recent research on SPCR in the setting of Indonesian economy has been growing in popularity, as researchers have been attempting to identify the causes of the occurrence in a number of financial and corporate-related aspects. For instance, Hamsyi et al. (2025) looked into how sharia compliance and ESG performance on the probability of market crashes, while Probohudono et al. (2021) and Hamidi et al. (2025) employed the impacts of intellectual capital and managerial skill on SPCR, respectively, through a mediating variable of company's financial performance. Furthermore, Zachro and Utama (2021) examined the familiy ownership role in the formation of influence of overworked directors.

However, there are limited studies that spesifically explore the moderating impact of financial constraints in terms of the connection involving corporate governance and SPCR in Indonesian context. Available literature in Indonesia is inclined to explore financial constraints or governance practices in various environments and result variables. As an example, Riesta and Septriana (2023) explores the role of good corporate governance in moving the impact of financial ratios on financial distress. Other studies show that financial constraints together with attributes of governance can moderate important corporate associations, including the behavior of tax avoidance (Silvera et al., 2022), and impact of financial constraints and corporate governance on environmental performance (Hanna & Hudayati, 2025). Even with this contribution, past studies have not

directly tested financial constraint as moderating variable in explaining the relationship between corporate governance and SPCR, which shows there is an gap that this research aims to fill.

Financial constraint defined as the challenge that firms face for getting external funds because of limited access to credit or high capital costs, financial constraint is a serious determinant of SPCR (Shelih & Wang, 2024). These constraints make information asymmetry more pronounced since the companies with a weak capacity to access financing are more susceptible to hoard innapropriate news to avoid bad market reactions that might further limit their ability to access capital (He & Ren, 2023). This is especially applicable to Indonesia where capital markets may be closed to collaborate with some firms, and where the quality of financial reporting might be undermined by financial pressure. Hadlock and Pierce's (2010) SA Index, which has been applied in the following research by He and Ren (2023), is used in this study to measure the financial constraint.

Skipping over financial constraints in studies linking corporate governance to SPCR may lead to an partial grasp of the whole dynamic. Existing research shows that significant financial constraint frequently hinders governance mechanism, where board independence are generally effective in preventing cash flow manipulation, but their effectiveness become ineffective when companies confront financial constraint (Usman et al., 2025). Bae et al. (2021) provide clear support for this finding, demonstrating that while high ESG ratings, which include the governance (G) dimension, typically mitigate the SPCR appearance, and this positive correlation decreases significantly in firms facing financial constraints. These results show that even when a company has solid governance systems, they are unable to prevent stock prices from dropping down when the companies are financially constrained.

In contrast to the failure of internal boards, Kurt et al. (2024) find that companies with limited funds strategically focus on better quality of audit. These firms will use more funds to ensure more reports are sent out within a shorter time to signal to investors with positive note. This type of strategy is essential to restore

confidence and make them able to obtain high-quality external financing. Farooq et al. (2022) argue that institutional ownership can overcome these constraints via enhanced monitoring.

He & Ren (2023) find that stock price decrease more and it becomes difficult to observe the financial transparency due to financial constraints. Therefore, not taking financial constraints in SPCR research could mean missing an important piece of the puzzle in understanding market volatility and behavior of companies. This suggests that financial constraint are not just secondary issue but a primary factor influencing market forces especially in emerging markets such as Indonesia. Given this critical points, there is a need to explore the role of financial constraints in SPCR. This intention of this research is to fill a research gap by incorporating the financial constraints as moderating variable in the study and present a more thorough understanding of the effect of financial condition on the SCPR.

To isolate spesific impacts, this study uses leverage and market to book ratio as control variables, following the methodological frameworks of previous research. While leverage may boost vulnerability to losses (Arhinful & Radmehr, 2023), this research complies to the approach of Cao et al. (2023) and Li et al. (2022), used leverage as a control and found a negative association with SPCR, implying that highly leveraged firms are less likely to crash. In terms of growth potential, this study utilizes the market to book ratio, which follows the control variable selection of Shelih and Wang (2024) with Dang and Nguyen (2021). These research discovered a positive link between MTB and the SPCR, stating that institution with high valuations are more vulnerable to SPCR. By including these control variables, it is possible to make sure that the capital structure or market valuation of the corporation does not obscure the consequence of corporate governance and financial constraint on collapse risk.

This research focuses on the consumer sector, encompassing both consumer cyclical and consumer non-cyclical industries posted on the Indonesia Stock Exchange (IDX). The sector of consumer is an ideal population for this study because it is inherently sensitive to public purchasing power, which has significantly declined and affected the demand structure for both elastic secondary products and essential requirements. This decline in demand, evidenced by a downward trend in core inflation since late 2023, and the accumulation of this pressure subsequently detonated in 2024, with BPS registering five consecutive months of deflation (Rachman, 2024), which resulted in cyclical sector was under the most pressure from January to June 2025, where the Consumer Cyclicals (IDXCYCLIC) index decreased by 14.03%, while the Consumer Non-Cyclicals (IDXNONCYC) index declined by 8.07% (Natalia, 2025).

Indonesia Stock Exchange (IDX) also recorded instability and opposite tendencies in performance of the consumer sector in the past five years, with consumer cyclical shrinking by 16.1% and non-cyclicals by 11.9% in 2020. This volatility was compounded in 2021 by a sharp divergence in which cyclicals recovered strongly with 21.2% growth and non-cyclicals struggled with a further 16% decline before reversing again in 2022 with non-cyclicals showing defensive performance increasing 7.9% over cyclicals increasing 5.5%, a low-growth divergence that has continued into 2023 with marginal growth of 0.8 in non-cyclicals compared to 3.5 in cyclicals (IDX, 2024).

However, the long-term reliability of non-cyclicals is increasingly questionable based on Q4 2024 data, which shows a steep 5-year performance decline of 18.72% and a surprisingly higher risk profile with a 5-year beta of 0.71 compared to the 0.63 beta of cyclicals, underscored by major corporate setbacks such as the 46.60% stock price drop in Unilever (UNVR) within a single year (IDX, 2024). This shows that even sectors that people usually think are stable or safe can be affected by sudden changes in the market and SPCR. These macroeconomic situation and sector volatility are a pressure to consumer sector companies. The strength of brand and pricing power are critical to the sustainability of the demand

in this industry, and they give managers in the sector a wide range of strategic choices to respond to the external shock by modifying prices, product repositioning, or by introducing new lower-priced products (Irwansyah et al., 2023). Although this kind of flexibility can be beneficial to the short-term performance, the success of these strategic choices becomes critical during economic stress as the firm tries to survive.

This is why the SPCR in the consumer sector is not only an indicator of macroeconomic weakness, but it also demonstrates possible malfunctioning of corporate governance systems in the control of managerial decisions in unfavorable situations (San et al., 2025). As the sector highly relies on corporate reputation, managers might have the greater motivation to conceal or postpone the reporting of negative news to maintain firm image, resulting in the silent accumulation of risk of firm-specific nature than can be immediately noticed by investors (Reichmann et al., 2022)

The years 2020-2024 is considered to discuss the efficacy of corporate governance mechanisms in this study. This period is overlappingg with the COVID-19 pandemic, which is reported to be a time of increased market volatility and high level of systematic risk (Dai et al., 2021), and this circumstances give one reason to suspect that the SPCR is being polluted by market-wide shocks. However, the effect of the COVID-19 on the SPCR is not necessarily similar in all settings. A research on the Chinese energy sector states that SPCR dropped during the COVID-19, as measured by the stock returns (weekly) of January 18, 2020 to April 24, 2020. This result implies that the economic reaction of the market to the pandemic can be different across industries and the local capital market structure (Huang & Liu, 2021).

Even so, to reduce this possible bias, this paper measure SPCR based on NCSKEW, the negative skewness of the firm specific returns. A larger NCSKEW figure is equivalent to the fact that a company is prone to a fall in prices when concealed bad news eventually trickles down to the market (Hamidi et al., 2025). In this way, isolating the behavior of abnormal firm-level returns filters market

returns and mitigates systematic shocks, including those that occur during the pandemic period. Besides, empirical studies indicate that the SPCR diffuses in the context of information asymmetry and managerial disclosure behavior, does not just spread in the context of concurrent market movements (Kong et al., 2023).

The pandemic and its long-term consequences significantly interfered with corporate processes and governance practices, and practically became the stress test of monitoring systems. These situations were further aggravated by tightening financial conditions and persistent downside risks, which contributed to the strengthening of financial constraints and management pressures of firms in the emerging markets, including Indonesia (Liao et al., 2023;IMF, 2024). This kind of environment might enhances managerial motivation to sustain positive news in the face of reduced consumer demand and economic insecurity, especially in the recovery phase in the period after that (Rachman, 2024). Based on this, the 2020-2024 period provides a holistic background to determine whether corporate governance mechanisms are still advisable when it comes to reducing the SPCR in the future when firms act based on different levels of financial constraints.

To the best of the author's knowledge, the moderating effect of financial constraint in the association between corporate governance, specifically board independence, institutional ownership, and audit quality on SPCR has not been studied explicitly in Indonesia before, making this study a novel contribution to the literature. This research, which focuses on consumer sector companies, presents a more extensive perspective of how financial constraints influence the probability of SPCR. This contribution is not only theoretically useful, but also practically relevant, since it will bring new perspectives on how financial constraints affect the effectiveness of governance systems in minimizing SPCR. Therefore, the proposed title for this research is **“Corporate Governance and Stock Price Crash Risk in Indonesian Consumer Sector Companies: The Moderating Impact of Financial Constraint,”** with empirical studies on companies in the consumer sector listed on the IDX from 2020 to 2024.

1.2 Research Problem

The statement of the problem for this research is outlined as follows:

1. Does board independence affect stock price crash risk in the Indonesian consumer sector?
2. Does institutional ownership have an impact on stock price crash risk of the consumer sector in Indonesia?
3. Does audit quality influence stock price crash risk in the Indonesian consumer industry?
4. Does financial constraint moderate the correlation of board independence on stock price crash risk in the Indonesian consumer sector?
5. Does financial constraint moderate the connection of institutional ownership on stock price crash risk in the Indonesian consumer industry?
6. Does financial constraint moderate the associaton of audit quality on stock price crash risk in the Indonesian consumer sector?

1.3 Research Objectives

Drawing from the previously stated research problem, the objectives of this research are as follows:

1. To assess the impact of board independence on stock price crash risk in the Indonesian consumer sector.
2. To examine the influence of institutional ownership on stock price crash risk of the consumer sector in Indonesia
3. To determine the effect of audit quality on the risk of stock price crashes in the Indonesian consumer industry.
4. To explore the moderating influence of financial constraint on the connection between board independence and stock price crash risk in the Indonesian consumer sector.
5. To analyze the moderating effect of financial constraint on the association between institutional ownership and stock price crash risk of the consumer sector in Indonesia

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6. To explore the moderating impact of financial constraint on the relationship between audit quality and stock price crash risk in the Indonesian consumer sector.

1.4 Research Benefits

1.4.1 Theoretical Benefits

This research contributes to the literature on corporate governance and processes of capital markets in the developing country such as Indonesia. The study provides detailed insights into the interplay between the governance mechanism and financial condition of the firms in order to analyze disclosure behavior and stock price crash risk (SPCR) by looking at how board independence, institutional ownership, and audit quality, in combination with financial constraint as a moderating variable affect SPCR. This addresses gap in the inconsistency of previous studies and prior Indonesian researches that have negleted the importance of financial constraint in triggering connection linking corporate governance and SPCR.

1.4.2 Practical Benefits

In practice, the findings of this research will provide helpful information to the corporate managers, investors, and the regulators. The results can be of great importance to corporate managers in the consumer sector in Indonesia who are tempted to conceal bad news when struggling with financial difficulties, but on the contrary the news should be disclosed openly to prevent the stock price fall to be seen in an abrupt manner. This study offers a useful guide when evaluating the risk profile of companies in the Indonesian consumer sector to enable investors make better decisions with regard to the quality of governance and financial stability of companies. The regulators and policymakers can also use the findings to enhance the structure of governance systems of the market, disclosure policies, and financial reporting principles to address the financial constraints of the firms. Such findings will eventually be useful in developing a more transparent, stable, and efficient capital market in Indonesia.

1.5 Scope of Research

To ensure focused and comprehensive research, this study sets specific boundaries for its variables and population. The independent variables (X) representing corporate governance are board independence, institutional ownership, and audit quality. The dependent variable (Y) is stock price crash risk (SPCR), which is measured using the Negative Coefficient of Skewness (NCSKEW). The moderating variable (Z) is financial constraint, which measure using the SA Index that helps figure out whether financial constraint either strengthens or weakens the impact of corporate governance. Leverage and market to book ratio are included as control variables. The samples for this study are consumer sector firms registered on the Indonesia Stock Exchange (IDX) with an observation period of five years, from 2020 to 2024.

1.6 Writing Systematics

This study comprises five chapters with a writing systematic in the following order:

CHAPTER I **INTRODUCTION**

This part explains the background of the research, problem formulation, research objectives, research benefit, scope of research, and systematics writing.

CHAPTER II **LITERATURE REVIEW**

This section covers the theories used and an explanation of each variable in this study. Morever, the development of hypotheses, previous studies, and the research framework are described in this chapter.

CHAPTER III **RESEARCH METHOD**

The contents of this section are the research design, population and samples, the type of data sources, the

methods used to collect data, the description variables, and the method of data analysis.

CHAPTER IV **RESULT AND DISCUSSION**

This chapter includes the descriptions of results, discuss the findings of data analysis and determines whether to reject or accept the research hypotheses, and compares it with the previous studies.

CHAPTER V **CONCLUSION**

This segment shows conclusions on the basis of the research outcomes, examines the implications of the study, mentions its limitations, and finally offers recommendations on future research.