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ABSTRACT

The aim of this study is to investigate the quality of earnings in terms of relevance and reliability of the company's performance and the market performance of the investors' perceptions that trigger reactions on market capitalization of going to public companies in Indonesia Stock Exchange. The company's performance can be seen from the operating profit (OP) while the market performance can be seen in other comprehensive income (OCI). The market capitalization (MC) is used to describe the annual reaction of investors. Referring to the international financial reporting standard (IFRS) this study was conducted to provide an overview on the Indonesian investor reaction to earning figures that the results are often inconsistent. Hypotheses were tested by time series and cross section and sample include 50 companies with the largest market capitalization on the Indonesia Stock Exchange during 2010 to 2014. The test results showed that there was a significant positive association between operating profit (OP) with market capitalization (MC) both in cross section test and time series test. But, there is not a significant positive association between other comprehensive income (OCI) with a market capitalization (MC). Wilcoxon sign test between OP and MC and between OCI to MC showed a significant difference, therefore, investors pay more attention on the company's operating profit (OP) than other comprehensive income (OCI). Thus the usefulness of IFRS adoption in IAS still need to be socialized to investors so, investors' decision can accommodates the economic realities in the market performance that contained OCI.

JEL Classification: L31; L33; M10.

Keywords: Operating Profit; Comprehensive Income; Market Capitalization; Indonesia.

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1. INTRODUCTION

Earnings quality indicates how earnings presented in the statement of profit/loss and other comprehensive income against the actual values. The main qualitative characteristics of financial statement presentation is relevant and reliable. Relevance indicates predictive power profit figures used for decision-making, while reliability showed management's performance in generating profit figures as a form of accountability to investors. Various arguments are often made profit figures presented in the financial statements to be less trusted by users, partly due to the arbitrary allocation which is mostly done in the calculation of the profit. Arbitrary allocation occurs in the calculation of cost of goods sold in the form of allocation of common costs of the service department to the production department and factory allocation of depreciation of fixed assets recorded as indirect production costs (add unit cost) when they are sold then they will be the cost of goods sold.

Arbitrary allocation also occurs in the calculation of operating expenses both in selling and marketing expenses and in general and administrative expenses. Related to the immediate recognition as advertising expenses and research & development expenses also affect the quality of earnings. Various things contained in the calculation of earnings the company should be considered carefully before used as a reference for decision making. Financial analysts must understand where the profit figures obtained. Hans Hoogervorst (IASB Chairman) (2014) suggested that a systematic relegation of unrealized profits or losses to OCI is extremely problematical. Moreover, where OCI is used to capture short-term 'market volatility' of long-term assets or liabilities, the information should not be ignored.

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