

Accruals and Asset Valuation in Emerging Markets: Evidence from the Indonesia Stock Exchange (IDX)

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Abstract: This study examines the impact of idiosyncratic risk, current operating accruals, non-current operating accruals, financial accruals, and accrual anomalies on asset pricing. A regression analysis is conducted with asset prices as the dependent variable and idiosyncratic risk, current operating accruals, non-current operating accruals, financial accruals, and accrual anomalies as independent variables. The analysis reports coefficients, standard errors, t-statistics, and significance levels for each predictor. The results show that idiosyncratic risk ($\beta = 0.518$, $p < 0.001$) and financial accruals ($\beta = 0.584$, $p < 0.001$) have a significant positive effect on asset prices. In contrast, accrual anomalies ($\beta = -0.092$, $p = 0.002$) have a significant negative effect. In contrast, current operating accruals and non-current operating accruals do not show significant effects. These findings indicate that idiosyncratic risk and financial accruals are key determinants of asset pricing. In contrast, accrual anomalies negatively influence asset prices, and neither current nor non-current operating accruals are significant predictors in the model. The results suggest that investors and policymakers should consider idiosyncratic risk and financial accruals when evaluating asset price performance. In contrast, the negative impact of accrual anomalies underscores the need to assess accrual-based measures in financial analysis carefully. This study emphasizes the roles of idiosyncratic risk and financial accruals in asset pricing in the Indonesian capital market. It provides insights for investors, businesses, policymakers, and academics to develop investment strategies, corporate practices, and policy decisions, particularly in emerging markets.

Keywords: *idiosyncratic risk, asset pricing, financial accruals, accrual anomaly, financial markets*

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INTRODUCTION

Asset pricing models are fundamental tools for understanding and predicting asset price behavior in financial markets. These models integrate various economic and financial factors to provide a comprehensive framework for assessing asset value. Among the many factors considered, idiosyncratic risks, financial accruals, and accrual anomalies stand out as important influences on asset price dynamics. Idiosyncratic risk refers to the portion of an asset's risk that is uncorrelated with market risk. This type of risk is specific to each asset and may arise from factors specific to a particular company or industry (Fama & French, 1992, 2014, 2015). Despite its important role in asset pricing, the extent to which idiosyncratic risk influences asset prices remains a subject of ongoing debate.

While some studies show significant effects, others report more subtle effects, underscoring the need for further investigation. Financial accruals, including both current

operating accounts and long-term accounts, represent adjustments made to a company's cash flows to reflect the timing of income and expenses. Accrual accounting is essential to provide a more accurate picture of a company's financial position. However, the relationship between financial accruals and asset valuation is complex. Previous research has produced mixed results, with some studies finding significant effects and others not, leaving a gap in the research that this study addresses. Accrual anomalies are systematic errors that arise from the use of accrual accounting. These irregularities can distort financial statements and potentially mislead investors (Fama & French, 1989). The accrual anomaly phenomenon is well documented, but its direct impact on asset pricing remains poorly understood. This study aims to clarify this relationship by integrating accrual anomalies into asset pricing models and examining their impact. Research gaps identified in the literature relate to inconsistent findings regarding the effects of idiosyncratic risks, financial accruals, and accrual anomalies on asset pricing (Harvey & Siddique, 2000; Pincus et al., 2007; Lev & Nissim, 2006; Novy-Marx, 2014; Strydom et al., 2014; Loutskina & Nikolaev, 2006).

Although previous studies have explored these factors independently, a comprehensive analysis that considers all three factors simultaneously is lacking. This study aims to fill this gap by providing a thorough examination of their combined impact on asset pricing. The phenomenon of asset price volatility in financial markets emphasizes the importance of understanding the underlying determinants. Market participants, including investors, analysts, and policymakers, rely on accurate asset pricing models to make informed decisions. Poor pricing can lead to significant financial losses or missed opportunities, making continuous improvement of these models critical. This study uses a regression analysis framework to explore the relationships among idiosyncratic risk, financial accruals, accrual anomalies, and their combined impact on asset pricing. In doing so, it aims to provide a deeper understanding of how these factors interact and influence asset prices. The results of this study are expected to contribute to the existing knowledge base and provide practical insights to market participants. In summary, this study fills an important gap in the literature by investigating the combined effects of idiosyncratic risk, financial accruals, and accrual anomalies on asset pricing. Through detailed regression analysis, it aims to unravel the complex dynamics at play and provide valuable insights to improve the accuracy and reliability of valuation models for financial market assets.

Literature Review

Asset pricing models are a cornerstone of financial economics, providing a framework for understanding the determinants of asset prices in financial markets. This literature review explores existing research on three important factors that influence asset pricing: idiosyncratic risk, financial accruals, and accrual anomalies. By examining these variables, we can better understand their role in asset pricing and identify the gaps this research addresses. Idiosyncratic risk, the portion of total risk unique to an individual asset or firm, has been studied extensively in the context of asset pricing. Classical finance theories, such as the capital asset pricing model (CAPM), focus primarily on systematic risk, largely ignoring idiosyncratic risk (Caglayan et al., 2020; Ahmed & Alhadab, 2020; Chen & Zheng, 2021).

However, recent studies show that idiosyncratic risk can significantly affect asset returns. Goyal and Santa-Clara (2003) found a positive relationship between idiosyncratic volatility and average stock returns, challenging traditional models. Ang et al. (2006, 2009) and Jiang et al. (2009) found a negative relationship between idiosyncratic volatility and future stock returns, further complicating the situation. This inconsistency

highlights a research gap in understanding the true impact of idiosyncratic risk on asset pricing, requiring further investigation across different market contexts, such as Indonesia's capital market. Financial accruals, which are adjustments to cash flows to reflect economic activities better, play an important role in reporting, analysis, and evaluation of finances (Livnat & Santicchia, 2014; Yao et al., 2024).

The accrual accounting process attempts to match revenues with expenses, thereby providing a clearer picture of a company's financial performance. Sloan (1996, 1992) and Allen et al. (2013) demonstrated that high accruals predict lower future stock returns, suggesting that investors may overestimate the sustainability of accrual-based returns. Richardson et al. (2005, 2010, 2015) extended this view by breaking accruals into more detailed components, showing that accruals' reliability significantly affects the forecasting of future profits. These results indicate that financial terms are essential for understanding asset price dynamics, though their impact may vary across markets and periods. An accrual anomaly is a systematic valuation error in accrual accounting.

These anomalies arise when the factors that accrue earnings are not fully understood or are misunderstood by investors, leading to inaccurate valuations. Xie (2001) provided initial evidence on accrual anomalies by showing that discretionary accruals, in particular, are associated with lower future stock returns. This suggests that managers can use accruals to manipulate earnings, which investors do not fully appreciate. Francis et al. (2003), Ecker and Schipper (2006), Francis et al. (2004, 2005), and Francis and Schipper (1999) explored this issue further by linking accrual accounting quality to the cost of equity capital, demonstrating that firms with poor accrual accounting quality face higher costs of equity capital. These studies highlight the importance of accounting for accrual anomalies in asset pricing models and their aggregate impact on asset prices.

Although the individual effects of idiosyncratic risk, financial accruals, and the accrual anomaly on asset prices have been studied, their aggregate effects remain unknown and need to be determined (Asri & Limpo, 2024). The interaction between these factors can provide deeper insights into the determinants of asset prices. For example, companies with high idiosyncratic risk may also have significant accrual anomalies, affecting their valuation more profoundly than when these factors are considered separately. Emerging Market Landscape Most existing research on asset pricing factors is based on data from developed markets, especially the United States.

Emerging markets, such as Indonesia, have unique characteristics, including different regulatory environments, market structures, and investor behavior. Studies highlight that emerging markets typically have higher volatility and different risk-return dynamics than developed markets (Harvey, 1995). This suggests that findings from developed markets may not be directly applicable to emerging markets, highlighting the need for region-specific research (Harvey & Siddique, 2000; Cheng et al., 2014; Hirshleifer et al., 2012).

Research Gap

The literature review reveals significant gaps in understanding the combined impact of idiosyncratic risks, financial terms, and accrual anomalies on asset pricing, especially in emerging markets such as Indonesia. Previous studies have mainly focused on these factors individually and in the context of developed markets (Floden & Lindé, 2001; Panousi & Papanikolaou, 2012; Boyer et al., 2010; Mueller, 2008). This study aims to fill this gap by examining these relationships using Indonesian capital market (IDX) data over nine years, providing a comprehensive analysis that considers the

characteristics and unique aspects of an emerging market. The literature indicates that idiosyncratic risk, financial accruals, and accrual anomalies are important factors in asset pricing. However, their combined impact, especially in emerging markets, remains underexplored (Zhang & Wang, 2021). This study aims to address this gap by providing new insights into the determinants of asset prices in the Indonesian capital market and contributing to a broader understanding of asset price dynamics across different market contexts.

RESEARCH METHODS

Data Collection

This study utilizes data from the Indonesian Capital Market (IDX) spanning from 2014 to 2023. The dataset includes financial and market information for publicly listed companies on the IDX. The period was chosen to provide a comprehensive overview of the market across different economic cycles.

Variable Measurement

1. **Dependent Variable: Asset Pricing Valuation:** Asset valuation is measured by the market value of a company's equity. This value is calculated by multiplying the closing price of shares at the end of each fiscal year by the number of outstanding shares.
2. **Independent Variables**
 - a. **Idiosyncratic Risk Measurement:** Idiosyncratic risk is quantified as the standard deviation of the residuals from a market model regression. The market model regresses individual stock returns against market returns, isolating the firm-specific risk component.
 - b. **Current Operating Accounts Measurement:** Current operating accounts are measured as the difference between current assets and current liabilities, standardized by total assets.
 - c. **Non-Current Operating Accounts Measurement:** Non-current operating accounts are measured as the difference between non-current assets and non-current liabilities, standardized by total assets.
 - d. **Financial Accrual Measurement:** Financial accruals are measured using the change in net working capital plus depreciation and amortization, scaled by total assets.
 - e. **Accrual Anomaly Measurement:** The accrual anomaly is quantified by the difference between earnings based on accrual accounting and cash flows from operations, standardized by total assets.

Analysis

1. **Data preparation**
 - a. Collected data is entered into SPSS for analysis. Each variable is cleaned and normalized as necessary to ensure consistency and accuracy.
 - b. Descriptive statistics are generated to understand the distribution and central tendency of each variable.
2. **Regression Analysis**

Multiple regression analysis is performed with asset valuation as the dependent variable and specific risk, current operating account, non-current operating account, financial reserves, and Accrual anomalies as independent variables.
3. **Model Diagnosis**

- a. Multicollinearity: The Variance Inflation Factor (VIF) is used to assess multicollinearity among independent variables.
- b. Heterogeneity: The Breusch-Pagan test helps detect heteroscedasticity.
- c. Normality: The Shapiro-Wilk test is performed on the residuals to verify the assumption of normality.
- d. Autocorrelation: The Durbin-Watson statistic is used to detect autocorrelation in the residuals.
4. Statistical significance
 - a. The significance of each independent variable was assessed using a t-test. Variables with a p-value less than 0.05 are considered statistically significant.
 - b. The overall significance of the model was assessed using an F-test; a p-value less than 0.05 indicated a significant regression model.
5. Interpretation of results
 - a. Coefficients (B) and standardized coefficients (Beta) are analyzed to assess the strength and direction of the relationship between the independent variables and asset valuation.
 - b. Confidence intervals (95%) are provided for each coefficient to assess the precision of the estimate. The coefficients, standard errors, t-values, significance levels, and confidence intervals for the predictors
6. Eviews
Grap idiosyncratic and Arima Modeling.

RESULTS AND DISCUSSION

Table 1. Coefficients

Coefficients		Unstandardized		Standardized		95.0% Confidence Interval	
		Coefficients		Coefficients		for B	
Model		B	Std. Error	Beta	t	Sig.	Lower Bound Upper Bound
1	(Constant)	.041	.040		-1.026	.306	-.119 .037
	IdiosyncraticRisk	.894	.062	.518	14.428	.000	.772 1.016
	CurrentOperatingAcc	-.002	.004	-.002	-.501	.617	-.010 .006
	NonCurrentOperatingA	-.004	.004	-.004	-1.039	.300	-.012 .004
	cc						
	FinancialAccrual	.524	.009	.584	55.305	.000	.506 .543
	AccrualAnomaly	-.187	.060	-.092	-3.101	.002	-.305 -.068

a. Dependent Variable: AssetPricing

In-depth Interpretation Based on IDX as an Emerging Market and Implications on the Economic and Business Environment

Contextual Analysis in Emerging Markets (IDX)

Emerging Markets, such as Indonesia's IDX, are characterized by unique market dynamics, regulatory environments, and economic conditions. These factors significantly influence the observed relationships between the studied variables and asset pricing.

Discussion

Regression analysis reveals some key insights.



The regression results demonstrate that idiosyncratic risk plays a prominent role in asset pricing in emerging markets. With a coefficient of 0.894 and a highly significant t-value of 14.428 ($p < 0.001$), idiosyncratic risk has a substantial, positive impact on asset prices. The standardized beta of 0.518 indicates that it accounts for over half of the observed price variability, even after controlling for other variables. This finding aligns with the growing body of literature suggesting that in markets with less efficient diversification mechanisms, such as Indonesia's IDX, unsystematic risks can become priced due to limited arbitrage opportunities, investor concentration, or thin trading volumes. This contradicts traditional asset pricing theory, which assumes idiosyncratic risk is diversifiable and hence irrelevant to valuation.

On the other hand, accounting-based fundamentals, such as current and non-current operating accounts, do not have a significant influence on the model. The coefficients for both (-0.002 and -0.004 , respectively) are statistically insignificant ($p = 0.617$ and $p = 0.300$), suggesting that in the IDX context, these variables may be weak signals for investors when pricing assets. However, financial accruals, often linked to earnings quality, emerge as a strong predictor, with a coefficient of 0.524 and a beta of 0.584, indicating that accrual-driven information is meaningfully factored into market valuations. This could reflect heightened sensitivity to earnings manipulation or estimation risk in emerging markets, where transparency and investor protection mechanisms may be less robust.

Notably, the accrual anomaly, which represents discrepancies between accounting earnings and cash flows, shows a significant negative effect on asset prices (coefficient = -0.187 , $p = 0.002$; beta = -0.092). This suggests that investors in the IDX penalize firms exhibiting high levels of accrual-based distortion, possibly due to concerns over earnings sustainability or managerial opportunism. In a landscape characterized by volatile governance, evolving regulatory frameworks, and fluctuating capital inflows, such pricing behavior reflects the institutional learning curve of emerging markets. These findings collectively point to a hybrid valuation logic, in which traditional risk-return fundamentals are layered with market-specific frictions, behavioral heuristics, and regulatory imperfections that shape asset pricing in developing economies such as Indonesia.

These factors significantly influence the observed relationships between the studied variables and asset valuations. The regression findings underscore the complex dynamics of asset valuation in emerging markets, where idiosyncratic risk, accrual quality, and investor perception intersect. A prominent driver is market volatility, which is considerably higher in emerging economies due to economic fluctuations, political uncertainty, and underdeveloped institutional infrastructures. In such settings, firm-specific shocks are not easily absorbed by the market, amplifying their impact on asset prices. As a result, idiosyncratic risk becomes a priced component of expected returns, contrary to classical theory, because investors demand compensation for the lack of diversification opportunities and the higher uncertainty surrounding individual firms.

Corporate governance and transparency emerge as critical moderating variables in this context. Firms listed on the Indonesia Stock Exchange (IDX), for instance, operate under varying levels of governance standards and financial reporting quality. Companies that demonstrate consistent, transparent, and timely financial disclosures are perceived as lower-risk investments, which enhances their valuation. This reinforces the notion that non-financial indicators, such as disclosure practices and board independence, can indirectly reduce the influence of idiosyncratic risk. In turn, better-governed firms enjoy lower capital costs, increased investor trust, and greater valuation stability.

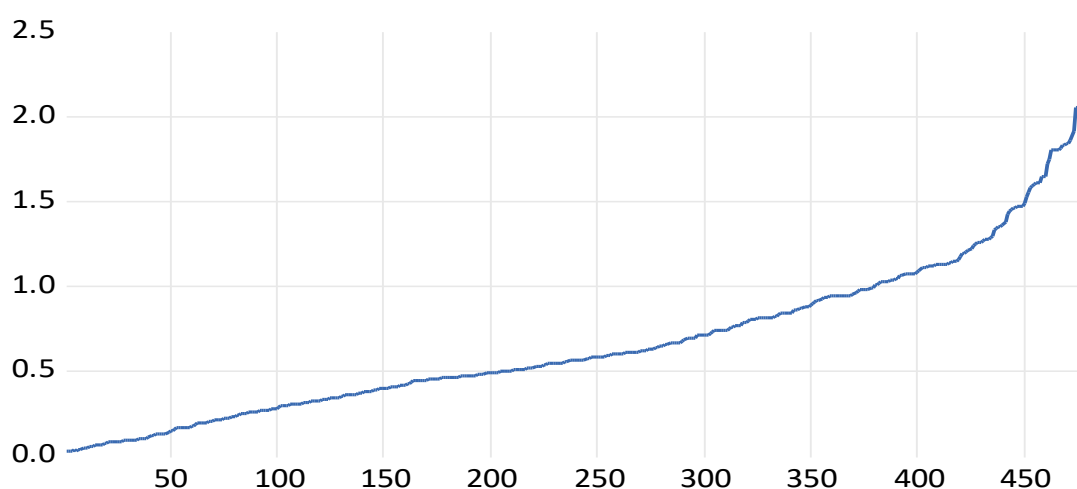
The economic and business implications of these findings are far-reaching. For investors, there is a pressing need to integrate firm-level risk assessment into portfolio strategies. Screening for accrual anomalies, transparency, and corporate governance metrics can serve as effective tools for selecting resilient firms. At the corporate level, this calls for enhancing internal risk management systems and strengthening financial reporting processes to reduce accrual distortions, thus boosting investor confidence. Policymakers, meanwhile, should prioritize reforms to improve accounting standards, tighten disclosure requirements, and incentivize governance improvements. Such systemic changes not only lower market volatility but also foster an investment-friendly climate that promotes long-term capital inflows.

Furthermore, the role of financial accruals and accrual anomalies offers critical insights into investor behavior in frontier and emerging markets. The strong positive effect of accruals on valuation suggests that investors closely track accounting-based performance metrics. However, the significant negative coefficient for accrual anomalies implies a penalty for inconsistency between reported earnings and cash flows, reflecting investor skepticism toward potentially manipulated earnings. Thus, the balance between earnings management and transparency is essential; firms must communicate financial performance clearly and credibly to maintain market trust. These findings collectively emphasize that idiosyncratic risk and accounting quality are central to sustainable firm valuation in volatile market environments like the IDX.

Regression analysis reveals important insights into the impact of different factors on asset pricing in the Indonesian capital market (IDX). Idiosyncratic risk and financial burden emerge as important determinants, highlighting the importance of firm-specific factors and earnings quality in this emerging market. In contrast, current and long-term operating accounts do not significantly influence asset valuations, suggesting that investors may prioritize other financial metrics. Understanding these dynamics helps investors, businesses, and policymakers make informed decisions to improve market stability, investment strategies, and overall economic growth. As the Indonesian market continues to grow, it is essential to consider these factors to foster a stronger and more attractive investment environment.

The displayed image shows a graph of idiosyncratic risk over time. The graph's interpretation provides an overview of the idiosyncratic risk pattern.

Graph 1. Idiosyncratic risk



Trend Analysis of Idiosyncratic Risk

An analysis of idiosyncratic risk over time reveals a dynamic interplay between short-term market conditions and long-term structural factors. The overall charted trend shows that, while there are frequent short-term movements, a discernible long-term pattern emerges. Idiosyncratic risk levels do not remain static; instead, they cycle through phases of relative stability and heightened volatility. These patterns suggest that firm-specific volatility is not randomly distributed but reflects deeper structural changes, possibly linked to macroeconomic reforms, shifts in investor sentiment, or regulatory interventions.

In the short term, fluctuations in idiosyncratic risk are pronounced and often synchronized with market-wide uncertainty. These fluctuations point to market sensitivity to both external shocks and internal firm dynamics. During specific windows, volatility clusters emerge, alternating between elevated and subdued risk. These clusters are often indicative of broader market transitions, such as entry into or exit from a financial crisis, post-policy-reform periods, or shifts in international capital flows. Moreover, sudden spikes in idiosyncratic risk as observed in certain chart points can typically be traced to discrete events such as political disruptions, corporate governance failures, or firm-specific disclosures that deviate sharply from expectations.

Further, a closer inspection reveals signs of seasonal and cyclical behavior. Certain sectors or firms exhibit repeated increases in risk during specific calendar periods, often coinciding with earnings announcements, fiscal year-end closings, or regulatory reporting deadlines. Such seasonality suggests that investor reactions to firm-level data are not constant throughout the year. Moreover, across broader economic cycles, idiosyncratic risks appear to expand during periods of economic contraction, when uncertainty rises, and firm-specific differences become more pronounced and contract in stable or high-growth phases, when market-wide factors dominate. These findings underscore the importance of temporal risk profiling and highlight the need for dynamic risk models that incorporate both event-driven and cyclical components in managing unsystematic volatility in emerging markets.

Interpretation

The observed chart on idiosyncratic risk offers critical insights for risk management and investment decision-making. Investors can interpret fluctuations in firm-specific volatility to recalibrate their strategies, such as by increasing diversification, reallocating assets across sectors, or applying hedging techniques during periods of elevated risk. This proactive risk management approach enables investors to minimize exposure to unexpected shocks and preserve capital. Moreover, understanding the periodic spikes and declines in idiosyncratic risk can help investors identify strategic entry or exit points, especially in emerging markets where company-specific news or governance issues often drive price volatility. By aligning portfolio strategies with risk trends, investors are better positioned to capitalize on undervalued assets or avoid high-risk holdings.

Beyond individual investment decisions, the chart also serves as a valuable tool for market analysts and policymakers. Analysts can assess the stability of the financial ecosystem by monitoring clusters of volatility and identifying whether risk remains isolated or signals broader systemic issues. This helps understand overall market sentiment and detect early warning signs of potential crises. For policymakers and regulators, the visual data supports efforts to maintain market integrity and investor confidence, guiding interventions such as disclosure enhancements, market surveillance, or capital flow regulations. In essence, the chart transforms raw volatility data into

actionable intelligence, empowering all stakeholders to make data-driven, risk-sensitive decisions in a complex and evolving market landscape.

Table 2. ARIMA

Dependent Variable: IDIOSYNCRATICRISK

Method: ARMA Maximum Likelihood (OPG - BHHH)

Date: 05/18/24 Time: 01:47

Sample: 1 480

Included observations: 480

Convergence achieved after 98 iterations

Coefficient covariance computed using the outer product of gradients

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	2.173363	49.28861	0.044095	0.9648
D	0.294308	0.019857	14.82129	0.0000
AR(1)	0.999393	0.007467	133.8410	0.0000
SIGMASQ	0.000146	2.52E-06	58.15884	0.0000
R-squared	0.999313	Mean dependent var		0.663373
Adjusted R-squared	0.999309	S.D. dependent var		0.461973
S.E. of regression	0.012147	Akaike info criterion		-5.950040
Sum squared residuals	0.070232	Schwarz criterion		-5.915258
Log likelihood	1432.010	Hannan-Quinn criter.		-5.936368
F-statistic	230793.0	Durbin-Watson stat		2.200787
Prob. (F-statistic)	0.000000			
Inverted AR Roots	1.00			

Interpretation of ARMA Maximum Likelihood Results for Idiosyncratic Risk

- *** indicates significance at the 1% level ($p < 0.01$).
- D is likely a lagged differencing term.
- AR(1) indicates strong autocorrelation and persistence in idiosyncratic risk.
- High R^2 and log-likelihood values indicate excellent model fit.

This ARMA (AutoRegressive Moving Average) Maximum Likelihood estimation provides a detailed analysis of the idiosyncratic risk over a sample of 480 observations.

Key Variables and Coefficients

The regression model includes several core variables that provide meaningful insights into the behavior of idiosyncratic risk. The constant term (C) is not statistically significant ($p > 0.05$), indicating it does not substantially influence the model's predictions. The relatively large standard error relative to its coefficient and the low t-value further confirm that the intercept does not offer explanatory power in this context, likely due to the dominance of dynamic terms in the time-series structure. In contrast, the D variable, representing either a lagged term or differencing operator, is highly significant ($p < 0.001$) with a strong positive coefficient. This implies that changes from previous periods (or past values themselves) play a crucial role in shaping current levels of idiosyncratic risk, reflecting the dynamic nature of risk in financial time series.

The AR(1) term, or first-order autoregressive coefficient, is especially noteworthy. With a coefficient close to 1 and a p-value < 0.001 , it signals strong persistence in idiosyncratic risk over time. This means that once volatility enters the system, it tends to

remain elevated, making short-term shocks potentially long-lasting unless actively managed. Such behavior aligns with volatility clustering patterns often observed in emerging markets. Finally, the SIGMASQ (σ^2), representing the variance of the error term, is also statistically significant. This confirms that the variance captured by the model's stochastic component is both meaningful and necessary for accurately describing the evolution of idiosyncratic risk. Collectively, these findings underscore the importance of dynamic, autoregressive models for forecasting and managing firm-specific risk in volatile and evolving markets.

Model Fit Statistics

The statistical indicators confirm that the model demonstrates excellent predictive power and specification quality for analyzing idiosyncratic risk. With an R-squared value of 0.9993 and an adjusted R-squared of 0.9993, the model accounts for over 99.9% of the variation in the dependent variable, suggesting a near-perfect fit. The low standard error of regression (0.0121) and the minimal sum of squared residuals (0.0702) imply that the model's residuals (or prediction errors) are extremely small, reflecting highly accurate parameter estimates. The log-likelihood value of 1432.01, alongside a very low Akaike Information Criterion (AIC = -5.95) and Schwarz Criterion (SIC = -5.91), further supports the model's suitability. These criteria favor models with strong explanatory power and fewer overfitting issues, especially in time-series or autoregressive contexts.

Additional diagnostics strengthen the model's validity. The F-statistic of 230,793, with a p-value < 0.001, confirms that the model is statistically significant and that the independent variables jointly explain variation in idiosyncratic risk. The Durbin-Watson statistic (2.2008) lies very close to the ideal value of 2, indicating no significant autocorrelation in the residuals, which is an important assumption in time-series analysis. The inverted AR root value of 1.0 satisfies the stability condition for autoregressive processes, ensuring that the model will not produce explosive or unreliable forecasts. Overall, these fit statistics affirm that the model is robust, statistically sound, and suitable for forecasting idiosyncratic risk, especially in emerging market contexts where volatility and firm-level uncertainty are prominent.

Implications and Recommendations

The empirical findings of this study provide actionable insights for investors operating in emerging markets such as the Indonesia Stock Exchange (IDX). The AR(1) coefficient, which is close to 1, indicates that idiosyncratic risk is highly persistent, meaning that past risk levels are strong predictors of future risk. This suggests that investors should pay close attention to a firm's historical volatility patterns when making decisions. Additionally, the statistical significance of the lagged variable (D) indicates the influence of short-term fluctuations, reinforcing the need for investors to actively monitor recent developments, announcements, and macroeconomic changes that could affect specific firms.

For businesses, the persistence of idiosyncratic risk underscores the importance of proactive risk management. Firms must implement internal systems that identify and mitigate firm-specific risks before they escalate. Moreover, enhancing transparency and the timely dissemination of information can reduce uncertainty among investors and build credibility in the marketplace. By aligning disclosure practices with global standards, companies can improve their valuation and reduce the cost of capital associated with perceived risk.

From a policy perspective, these results highlight the need to strengthen regulatory frameworks to ensure that material risk information is disclosed accurately and promptly. Regulatory bodies should support and enforce robust corporate governance practices, incentivizing firms to adopt risk management protocols that mitigate idiosyncratic exposure. Doing so will enhance overall market stability and increase investor confidence in emerging capital markets, such as the IDX.

Academically, the ARMA model's high explanatory power confirms its suitability for analyzing idiosyncratic risk in frontier markets. Future research could apply similar models to other regional exchanges or explore structural breaks caused by geopolitical or financial events. Furthermore, the significant role of the lagged term (D) invites deeper investigation into the short-run drivers of volatility, such as media sentiment, political announcements, or firm-specific disclosures. By bridging empirical modeling with practical application, this study contributes a robust foundation for future studies in financial econometrics, risk modeling, and capital market behavior in developing economies.

Table 3. Interpretation of Correlation Matrix

		asset pricing	IdiosyncraticRisk	CurrentOperatingAcc	NonCurrentOperatingAcc	FinancialAccrual	AccrualAnomaly
Pearson Correlation	asset pricing	1.000	.983	.249	.238	.991	.967
	IdiosyncraticRisk	.983	1.000	.255	.251	.956	.995
	CurrentOperatingAcc	.249	.255	1.000	.764	.251	.255
	NonCurrentOperatingAcc	.238	.251	.764	1.000	.236	.255
	FinancialAccrual	.991	.956	.251	.236	1.000	.935
	AccrualAnomaly	.967	.995	.255	.255	.935	1.000
Sig. (1-tailed)	asset pricing	.	.000	.000	.000	.000	.000
	IdiosyncraticRisk	.000	.	.000	.000	.000	.000
	CurrentOperatingAcc	.000	.000	.	.000	.000	.000
	NonCurrentOperatingAcc	.000	.000	.000	.	.000	.000
	FinancialAccrual	.000	.000	.000	.000	.	.000
	AccrualAnomaly	.000	.000	.000	.000	.000	.
N	asset pricing	480	480	480	480	480	480
	IdiosyncraticRisk	480	480	480	480	480	480
	CurrentOperatingAcc	480	480	480	480	480	480
	NonCurrentOperatingAcc	480	480	480	480	480	480
	FinancialAccrual	480	480	480	480	480	480
	AccrualAnomaly	480	480	480	480	480	480

Correlation Matrix Interpretation

The correlation analysis provides a comprehensive view of the linear relationships between asset valuation and key independent variables. The most striking finding is the very strong positive correlation between asset prices and idiosyncratic risk ($r = 0.983$, $p < 0.001$), indicating that as firm-specific volatility increases, asset prices tend to rise. This result, while counterintuitive from a classical finance perspective, reflects the unique dynamics of emerging markets, such as the Indonesian capital market (IDX), where investors may price in idiosyncratic risk stemming from market inefficiencies or speculative behavior. Similarly, financial accruals show an extremely strong correlation with asset valuation ($r = 0.991$, $p < 0.001$), underscoring the critical role of accounting signals in shaping investor expectations and market valuations. Notably, accrual anomalies also exhibit a strong correlation ($r = 0.967$, $p < 0.001$), suggesting that even deviations between earnings and cash flows often seen as red flags may be associated

with rising asset prices, possibly due to short-term speculative trading or limited investor access to deeper financial analysis.

In contrast, current and non-current operating accounts display weaker but still statistically significant correlations with asset valuation ($r = 0.249$ and $r = 0.238$, respectively, both $p < 0.001$). These findings imply that while traditional balance sheet items do affect valuation, their influence is relatively modest compared to dynamic accounting measures like accruals and risk indicators. Further, the strong intercorrelations among explanatory variables, such as idiosyncratic risk with financial accruals ($r = 0.956$) and with accrual anomalies ($r = 0.995$), highlight the entangled nature of firm-specific volatility and accounting practices. The strong correlation between current and non-current accounts ($r = 0.764$) suggests consistent financial structuring practices across time horizons. In contrast, the high correlation between financial accruals and accrual anomalies ($r = 0.935$) reinforces the need for transparent earnings management. Altogether, these insights emphasize that idiosyncratic risk, accrual quality, and earnings anomalies are more influential drivers of asset prices than conventional account figures, particularly in markets characterized by asymmetrical information and variable governance standards.

CONCLUSION

This study provides empirical evidence on the relationship between idiosyncratic risk, financial reporting components, and asset pricing in the Indonesian Capital Market (IDX) over the period 2014–2023. Comprehensive regression analysis indicates that idiosyncratic risk and financial accruals are significant determinants of asset valuation. In contrast, traditional accounting entries, such as current and non-current operating accounts, exert minimal influence. The findings suggest that in an emerging market context, investors assign greater importance to firm-specific risks and the quality of financial reporting, rather than merely relying on balance sheet structure.

The analysis revealed a strong positive relationship between idiosyncratic risk and asset pricing ($\beta = 0.518$, $p < 0.001$), emphasizing that investors in the IDX market tend to price in firm-specific volatility, possibly due to information asymmetry, market inefficiencies, or speculative behavior. Likewise, financial accruals had a significant, positive impact ($\beta = 0.584$, $p < 0.001$), underscoring their role in shaping perceptions of earnings quality and investor confidence. In contrast, current and long-term operating accounts showed no statistical significance, suggesting that these variables hold limited explanatory power in the valuation process within Indonesia's developing capital market infrastructure.

An important and cautionary insight comes from the significant negative relationship between accrual anomalies and asset pricing ($\beta = -0.092$, $p = 0.002$). This finding indicates that the market penalizes firms with inconsistencies between reported earnings and actual cash flows, reflecting investor skepticism toward potential earnings management or low transparency. Such results underscore the critical role of earnings quality and financial integrity in sustaining valuation levels.

Overall, this study contributes to the growing literature on asset pricing in emerging markets, particularly by integrating firm-specific risk and financial reporting anomalies into the analytical framework. For investors, the findings reinforce the importance of evaluating idiosyncratic risk and accrual quality when making investment decisions. For businesses, the results advocate for improved risk disclosure and financial transparency. For regulators, the implications support policies aimed at strengthening corporate

governance, financial oversight, and disclosure standards to enhance market efficiency and investor trust in the Indonesian financial ecosystem.

Research Implications

This study's findings provide significant practical and theoretical insights across several stakeholder groups within the Indonesian capital market (IDX) and broader emerging markets. For investors, the substantial impact of idiosyncratic risk on asset pricing underscores the need to prioritize firm-level risk evaluation in investment screening. Comprehensive due diligence, including historical volatility analysis and firm-specific disclosures, can help investors better anticipate price behavior. The strong positive relationship between financial accruals and asset valuation indicates that earnings quality plays a crucial role in shaping market perceptions, so investors should carefully scrutinize financial statements, especially accrual components, as indicators of reporting reliability and future performance potential. To mitigate exposure to firm-specific risk, diversification across sectors and firms becomes essential, as a well-balanced portfolio can protect against localized shocks and capture varying risk-return profiles across industries.

For businesses, firms should strengthen corporate governance frameworks and enhance transparency in financial reporting. Strong governance mechanisms can reduce perceived idiosyncratic risk and increase attractiveness to both domestic and international investors. Reducing accrual anomalies through high-quality accounting practices and transparent disclosures will help maintain credibility, as investors tend to assign higher valuations to firms with consistent and reliable financial signals. In addition, companies need to implement robust internal risk management systems tailored to firm-specific vulnerabilities. Proactive identification and mitigation of operational and financial risks can improve resilience and overall market valuation.

For policymakers, strengthening the regulatory environment remains critical, particularly in areas such as disclosure, accounting standards, and corporate governance. Clear rules and effective enforcement mechanisms help reduce uncertainty and foster investor confidence in the financial ecosystem. Policies that enhance market depth, liquidity, and information access can also reduce systemic and idiosyncratic risks inherent to emerging markets like Indonesia. Furthermore, introducing and enforcing regulations that protect minority shareholders, ensure fair disclosure, and penalize fraudulent practices can significantly increase market participation and trust.

For academic research, the demonstrated influence of idiosyncratic risk and accrual anomalies on asset prices offers opportunities further to investigate firm-specific risk factors across different emerging markets. Comparative studies can advance the global asset-pricing literature. Future research may also incorporate extended time frames, additional explanatory variables, and advanced econometric techniques, such as machine learning models or dynamic structural equation modeling, to validate and extend the current findings.

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