

How Firm Characteristics Shape Earnings Quality: Evidence from Indonesian Manufacturing Firms

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ABSTRACT

This study aims to analyze the effect of firm size, profitability, and liquidity on earnings quality in manufacturing companies within the industrial sector listed on the Indonesia Stock Exchange (IDX) during the 2020–2023 period. Earnings quality is a multidimensional concept that reflects how reported earnings are reliable and relevant for stakeholders in making economic decisions. In this context, agency theory is the foundation to explain potential conflicts of interest between managers and shareholders in financial reporting practices. The sample was selected using a purposive sampling method based on specific criteria, and the data were analyzed using multiple linear regression. Classical assumption tests indicate that the data meet the requirements for normality, show no multicollinearity or autocorrelation, and satisfy the assumption of homoscedasticity. Regression results show that firm size does not significantly affect earnings quality ($p > 0.05$), while profitability and liquidity have a negative and significant effect on earnings quality ($p < 0.05$). The coefficient of determination (R^2) of 14.1% indicates that the three independent variables explain only a small portion of the variation in earnings quality. The study's implications highlight the importance of monitoring managerial practices, particularly in companies with low profitability and liquidity, to prevent earnings manipulation and enhance investor trust. The findings also encourage regulators to strengthen financial reporting transparency policies and provide valuable insights for investors to evaluate financial statements critically.

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1. Introduction

Earnings quality is a multidimensional concept that reflects how reported earnings provide valuable and relevant information for stakeholders in making economic decisions. Stakeholders rely on earnings reports for analyzing the business value (Driskill et al., 2020; Flugum & Souther, 2025). It encompasses the accuracy and reliability of reported earnings and their sustainability and predictive power. High earnings quality indicates that profits are generated from sustainable and reliable operational activities, thus providing an accurate picture of a company's financial condition (Zhang et al., 2025). On the other hand, low-quality earnings, which non-operational factors or opaque accounting policies may influence, can mislead and harm investors in their decision-making

process (Liao & Errico, 2023). Therefore, investors and stakeholders need to understand the quality of earnings in financial reports in order to make well-informed and reliable investment decisions.

Companies with high earnings quality tend to be more attractive to investors because the reported profits reflect sustainable and stable performance. Financial statements give investors greater confidence in the company's solid long-term growth prospects, ultimately increasing stock valuation and potential shareholder returns (Salehi et al., 2023). Moreover, companies with high earnings quality typically demonstrate better cost and revenue management and compliance with applicable accounting standards. These factors strengthen the company's position in the market, thereby fostering stronger relationships with investors and other stakeholders.

However, one case that illustrates low earnings quality is the financial reporting of PT Indofarma Tbk (INAF) and its subsidiaries during the 2020–2023. During this period, the public and investors frequently questioned the company's financial management, especially regarding the transparency of its financial statements (Aprian & Yustisia, 2022). Furthermore, a significant case that emerged was the alleged manipulation of financial reports discovered in May 2024, with findings of irregularities in transaction records and revenue recognition inconsistent with prevailing accounting regulations. This manipulation was significant, amounting to IDR 371.8 billion, seriously damaging the company's credibility and integrity in the eyes of investors. Additionally, the company had previously been fined IDR 500 million in 2001 due to financial data presentation that did not comply with existing policies.

The lack of clarity and accuracy in PT Indofarma Tbk's financial disclosures poses a risk of long-term losses for the company. This could affect the company's stock value, influencing investor interest. When investors perceive a company's financial statements as untrustworthy, they are likely to avoid or even withdraw their investments, leading to a decline in liquidity and market valuation. Moreover, companies may also face legal sanctions and penalties from capital market authorities, further damaging their public image. This case highlights the importance of high-quality earnings and transparency in financial reporting to maintain positive relationships with investors and other stakeholders, as well as to ensure the company's sustainability.

Firm size is one of the aspects that affects earnings quality and financial statements (Solikhah et al., 2022). Larger companies generally have more financial, infrastructure, and managerial resources that enable them to produce more transparent and accurate financial data (Sambo et al., 2023; Sánchez-Infante Hernández et al., 2020). Furthermore, larger companies are often subject to stricter monitoring by capital market authorities and regulators, making them more likely to comply with applicable accounting standards (Wang & Zhao, 2020). Additionally, large firms usually have better access to capital markets (Halling et al., 2020), and are more capable of managing operational risks (Ozdemir et al., 2022), affecting the quality of reported earnings. Conversely, small or medium-sized enterprises may face greater challenges in financial management and resource limitations, potentially impacting the quality of their financial statements. Therefore, firm size is often closely associated with reliable earnings quality.

Profitability also significantly contributes to reported earnings quality (Zhang et al., 2025). Efficient resource management enhances profitability (Djolafo, 2022), with earnings quality emerging as a key driver of long-term bank performance efficiency (Kweh et al., 2024). Earnings strength alone does not ensure high-quality reporting or comprehensive corporate transparency, as profitability has limited influence on integrated reporting (Darminto et al., 2024). Profitability exhibits a strong and significant association with stock returns, while earnings quality measures show no significant predictive power (Fonou-Dombeu et al., 2024). On the contrary, companies with low or unstable profitability may rely on non-operational transactions (Sufiati & Pura, 2023), such as asset sales or other income sources, to boost their reported profits. Firms with low profitability exhibit a higher tendency to shift classification, thereby compromising earnings quality without strong external governance mechanisms (Zudana & Opore, 2025). This can reduce the quality of earnings, as such profits are not derived from ongoing business activities. In low-profitability firms, expecting future disclosures by managers reduces firm value and manager earnings due to lower initial liquidity (Fu & Trigilia, 2024). Thus, profitability is important in evaluating financial data quality and providing a clear picture of a company's financial strength.

Liquidity, which measures a company's ability to meet its short-term obligations, influences financial statement quality and transparency (Donkor et al., 2025). Companies with good liquidity can manage their cash flow more efficiently, reducing the need for manipulation or inaccurate entries in financial reports. These companies tend to be more financially stable (Atanasova & Willeboordse, 2025), having enough cash to cover liabilities without relying on short-term debt or altering income and expense records (Barik & Chakrabarty, 2025). Conversely, companies with liquidity issues may be forced to delay payments or adjust financial figures to create a declining profitability (Alemu & Worku, 2025). For example, Low liquidity during a recession leads to declining asset prices and corporate earnings, thereby increasing buyers' expectations of higher returns (Doshchyn, 2025). Another example is a finding of (Tian & Park, 2024) that the significant decline in liquidity due to implementing the environmental protection tax reduces firms' short-term liquidity. Hence, healthy liquidity is essential to ensure that financial data accurately reflects the company's financial condition.

Despite numerous studies examining the influence of profitability, firm size, and liquidity on earnings quality in financial reports, there remains a lack of comprehensive understanding regarding the interaction among these factors, particularly in companies with low earnings quality. Most prior research has focused on large companies with transparent financial statements, while in-depth studies of companies facing transparency and earnings quality challenges are still limited. Therefore, this study examines the effect of firm size, profitability, and liquidity on earnings quality as reflected in financial reports. By analyzing the relationships among these three factors, deeper insights can be gained into how company characteristics affect the quality of reported earnings. The findings of this study are expected to help investors and stakeholders make more informed investment decisions based on accurate and reliable data. Additionally, the study contributes to enhancing the transparency of corporate financial reporting, which in turn encourages better and more accountable financial management practices.

Agency Theory

Agency theory suggests that managers, acting as agents of the shareholders, may prioritize their interests (Löhde et al., 2021; Solomon et al., 2021). This can lead to actions that maximize short-term profits at the expense of long-term sustainability and comprehensive reporting (Edmans et al., 2022). The traditional paradigm of annual reports as instruments exclusively directed towards shareholders and investors must transform fundamentally.

This theory asserts that such conflicts can influence decision-making in company management, including the transparency of financial reporting (Kasbar et al., 2023). In the context of financial transparency and financial reporting, information asymmetry arises between the internal parties (agents) and external parties (principals) (Salehi et al., 2023). Information asymmetry can influence the transparency and accuracy of the financial statements. Therefore, it is important to ensure that the management as an agent act in the company's best interest (Boivie et al., 2021). Aggressive earnings management can distort the perception of a company's long-term success. For instance, companies with high earnings quality tend to demonstrate transparent management practices, which help reduce agency costs and minimize the risk of financial statement manipulation that could harm investors. Understanding agency theory is thus essential for identifying potential issues affecting reported earnings quality and designing policies that promote transparency and accountability in financial reporting.

In agency theory, the relationship between firm size, profitability, liquidity, and earnings quality is explained through potential conflicts of interest between shareholders and managers. Large firms typically have more resources and are subject to greater scrutiny, encouraging higher transparency and reducing earnings manipulation. High profitability reflects consistent earnings representing actual performance, whereas firms with low profitability may be more inclined to manipulate earnings. Likewise, good liquidity allows companies to meet short-term obligations without altering financial reports, enhancing transparency. Altogether, these three variables influence the quality of reported earnings, and understanding their relationships is essential for developing policies that improve financial reporting transparency and accountability.

Company Size and Earnings Quality

Firm size refers to the scale or magnitude of a company, which is often measured using various indicators such as total assets, revenue, market capitalization, or number of employees. Large firms typically possess more resources (Mansour et al., 2023)—financial, infrastructural, and managerial—that allow them to operate more efficiently (Hughes, 2008) and produce transparent and accurate financial data (Roszkowska, 2021). They are also better equipped to comply with regulatory standards due to greater capacity in oversight and adherence to strict accounting rules (Amirapu & Gechter, 2020; Breuer, 2021).

Moreover, larger companies are often under more intense supervision from regulators and capital market authorities, making them more likely to present trustworthy financial statements that reflect actual conditions. Conversely, small or medium-sized enterprises may face resource limitations regarding personnel, capital, and management systems (Mendy, 2021), which can hinder their ability to produce equally accurate and transparent financial data (Kamall Khan et al., 2022). These constraints may lead to suboptimal financial management and potential inaccuracies in information disclosure. As a result, firm size is closely associated with the quality of financial reporting, with larger firms generally better positioned to maintain credibility and accuracy in their financial statements.

H1 : Company Size affect Earnings Quality

Profitability and Earnings Quality

Profitability is one of the key indicators that illustrates the extent to which a company can generate profit from its activities. It reflects the company's effectiveness in managing resources, such as income and expenses, to achieve optimal profits (Bhattacheryay, 2023). High profitability indicates that the company can maintain long-term stability (Alshehadeh et al., 2024). In contrast, low profitability may indicate inefficiencies in operational strategy or resource management, potentially impacting the quality of reported earnings. In such situations, companies may rely on non-operational income sources to boost profit figures, which can distort the actual financial condition and undermine credibility in the eyes of investors (Al-Otaibi et al., 2024). Therefore, profitability serves as a performance indicator and a tool to evaluate the financial resilience and long-term stability of the company in the market.

H2 : Profitability affect Earnings Quality

Liquidity and Earnings Quality

Liquidity refers to a company's ability to quickly convert assets into cash to fulfill short-term financial obligations. It reflects how efficiently an entity can balance liquid assets with financial liabilities that are due shortly. High liquidity indicates strong cash flow management, enabling smooth operations without disruption from urgent debt or payment needs.

Conversely, low liquidity can lead to difficulties in liquidating assets or mobilizing funds quickly, potentially exacerbating financial issues and damaging the company's reputation in the market. In such cases, companies may be forced to seek external financing or loans that could further strain their financial condition. Therefore, maintaining healthy liquidity is crucial to ensure companies can endure unexpected situations and meet financial commitments on time. In other words, liquidity is not merely a financial indicator but also a critical factor determining long-term sustainability and the company's credibility in the eyes of creditors, investors, and other stakeholders.

H3 : Liquidity affect Earnings Quality

2. Research Method

This study aims to analyze firm size, profitability, and liquidity variables in relation to earnings quality. The research focuses on companies listed on the Indonesia Stock Exchange (IDX) from 2020 to 2023. The population of this study consists of manufacturing companies in the industrial sector listed on the IDX during the same period. Population refers to a group of subjects and objects that

are the focus of the research and possess specific characteristics relevant to the study. A sample of this population is selected to represent companies that meet specific criteria. A sample is a subset of the population that serves as its representative. To determine the sample, this study employs a purposive sampling method based on the following criteria:

1. Manufacturing companies in the industrial sector listed on the IDX throughout the observation period (2020–2023).
2. Companies that consistently published their financial data during the years 2020–2023.
3. Companies that use the Indonesian Rupiah (IDR) as the currency in their financial reporting.
4. Companies that did not report losses during the observation period (2020–2023).

To test the hypotheses, the study utilizes multiple linear regression analysis. This technique analyzes and measures the strength and direction of the relationships between each variable. The purpose of the hypothesis testing is to observe whether each independent variable has a statistically significant effect on the dependent variable. Each hypothesis—whether the first, second, or third—is tested using the individual parameter significance test (t-test) to determine whether each independent variable significantly affects the dependent variable (earnings quality). This process ensures that the research results provide strong evidence regarding the influence of each factor and reveal deeper insights into how these variables affect the quality of earnings reported by companies. Therefore, the hypothesis testing is expected to offer a clear understanding of the dynamics that impact earnings quality and contribute meaningfully to broader research in accounting and finance.

3. Results

This section presents the findings obtained from the study, along with an in-depth analysis of the relevant results. The discussion includes the interpretation of the data collected throughout the research process. The analysis aims to provide a comprehensive understanding of the phenomenon under investigation and to draw meaningful conclusions from the results. By examining the relationships among the variables and interpreting the statistical outputs, this section highlights the implications of the study’s findings for both theory and practice. The discussion also seeks to explain how the results align with or differ from previous research, offering insights into the underlying factors that influence earnings quality in relation to firm size, profitability, and liquidity.

Table 1: Descriptive Statistical Test Results

	N	Minimum	Maksimum	Mean	Std.Deviation
Company Size	55	12.73	28.91	24.2936	5.25364
Profitability	55	.00	.24	.0851	.05640
Liquidity	55	.016	8.58	2.0736	1.19188
Earnings Quality	55	.84	2.95	1.5407	.55332
Valid N (Listwise)	55				

Source: Secondary Data Processed by SPSS, 2025

Table 1 presents the descriptive statistics for the variables analyzed in this study. The mean value of firm size is 24.2936, with a maximum of 28.91, a minimum of 12.73, and a standard deviation of 5.25364. These figures indicate substantial variability in firm size among the sampled companies, which may reflect differences in operational scale and resource capacity. Larger firms are likely to possess more extensive infrastructure and assets, while smaller firms may operate with more constrained resources. For the profitability variable, the maximum value is 0.24, the minimum is 0.12, and the standard deviation is 0.05. Although the range is relatively narrow and the maximum value modest, the low standard deviation suggests that the firms in the sample exhibit similar levels of profitability. This points to a relatively homogeneous financial performance in terms of profit generation. The liquidity variable shows a maximum value of 2.0736, a minimum of 0.00, and a standard deviation of 1.191. These results indicate considerable variation in liquidity among the firms, suggesting that while some companies maintain strong liquidity positions, others

may rely more heavily on external sources of financing. This variation reflects differing levels of financial flexibility within the sample. Lastly, the earnings quality variable records a maximum value of 2.95, a minimum of 0.84, and a standard deviation of 0.55. The moderate dispersion in this variable implies notable differences in earnings performance among the firms. Such variation may be attributable to differences in accounting policies, managerial discretion, and operational efficiency across the observed companies.

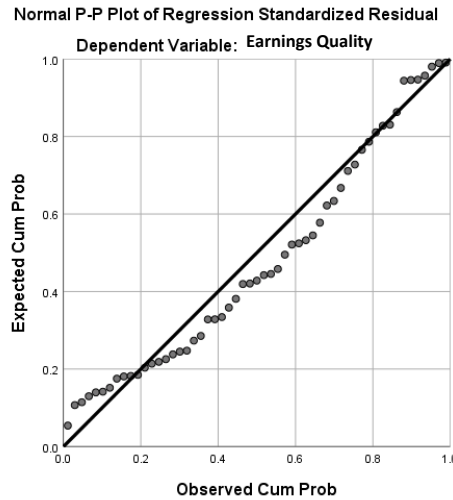


Figure 1. Test Classic Assumptions with P-Plot

As illustrated in Figure 1, the dependent variable—earnings quality—exhibits a normal distribution, as evidenced by the P-P Plot in which the data points closely align with the diagonal reference line. This alignment indicates that the residuals are normally distributed, thereby meeting one of the fundamental assumptions of linear regression analysis. In addition to the visual assessment provided by the P-P Plot, a one-sample test was performed as part of the classical assumption testing. This statistical test is commonly employed to evaluate normality, particularly in determining whether a sample originates from a specified distribution or whether its mean significantly deviates from a known value. The outcomes of the one-sample test reinforce the visual interpretation from the P-P Plot, affirming that the data satisfy the normality assumption. This confirmation ensures the appropriateness of the dataset for conducting regression analysis and subsequent hypothesis testing.

Table 2. One-Sample Test – Classical Assumption (Normality Test)

		Unstandardized Residual
N		55
Normal Parameters ^{a,b}	Mean	0,0000000
	Astd.Deviation	.48573754
Most Extreme Differences	Absolute	.108
	Positive	.108
	Negative	-.082
Test Statistic		.108
Asymp. Sig. (2-tailed)		160

Source: Secondary Data Processed by SPSS, 2025

As presented in Table 2, the Asymptotic Significance (2-tailed) value is 0.160, which exceeds the threshold of 0.05. This result indicates that the residuals are normally distributed. Consequently, the assumption of normality is satisfied, confirming that the data is appropriate for subsequent statistical procedures, including regression analysis and hypothesis testing.

Table 3. Multicollinearity Test

		Collinearity Statistics	
Model		Tolerance	VIF
1	Company Size	.953	1.050
	Profitability	.847	1.180
	Liquidity	.869	1.151
Dependent Variable: Earnings Quality			

Source: Secondary Data Processed by SPSS, 2025

As shown in Table 3, all independent variables in this study satisfy the assumption of no multicollinearity. The Firm Size variable has a Tolerance value of 0.953 and a Variance Inflation Factor (VIF) of 1.050. The Profitability variable reports a Tolerance of 0.847 and a VIF of 1.180, while the Liquidity variable yields a Tolerance of 0.869 and a VIF of 1.151. Since all Tolerance values exceed the commonly accepted minimum threshold of 0.10 and all VIF values fall below the critical limit of 10.00, it can be concluded that multicollinearity is not present among the independent variables. This implies that the variables are sufficiently independent and do not exhibit problematic linear interrelationships, thereby fulfilling an essential classical assumption for the validity of multiple linear regression analysis.

Table 4. Autocorrelation Test

Model	R	R. Square	Adjusted R Square	Std. Error of the Estimate	Durbin-watson
1	.375 ^a	.141	.089	.56893	1.732

Source: Secondary Data Processed by SPSS, 2025

The autocorrelation test results are presented in Table 4, utilizing the Durbin-Watson (DW) statistic, which yielded a value of 1.732. To interpret this result, reference is made to the Durbin-Watson critical values table, considering the number of observations (N = 55) and the number of independent variables (k = 3) at the 5% significance level. Based on the table, the lower bound (dL) is 1.4523, the upper bound (dU) is 1.6815, and the value of 4 - dU is 2.3185. The criterion for the absence of autocorrelation is satisfied when the DW statistic falls between dU and 4 - dU. In this case, the DW value of 1.732 lies within the interval 1.6815 < DW < 2.3185. Therefore, it can be concluded that the dataset does not exhibit autocorrelation, thereby fulfilling another classical assumption required for the validity of regression analysis.

Table 5. Multiple Linear Regression Test

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	1.889	.331		5.710	.000
	Company Size	.008	.013	.073	.577	.566
	Profitability	-2.873	1.310	-.293	-2.193	.033
	Liquidity	-.140	.061	-.301	-2.279	.027
Dependent Variable: Earnings Quality						

Source: Secondary Data Processed by SPSS, 2025

It is known that the multiple linear regression equation:

$$Y = a + b_1X_1 + b_2X_2 + b_3X_3$$

The Multiple Linear Regression Equation obtained from the test results is as follows:

$$Y = 1.889 + 0.008X_1 - 2.873X_2 - 0.140X_3$$

Hypotheses Testing

The constant value of 1.889 is assumed if the independent variable is 0 (constant), so the dependent variable is worth 1.889. Then the coefficient of regression X1 is positive 0.008, it is assumed that if X1 increases, so that Y increases and vice versa. The X2 coefficient value is negative in the amount

of -2.873. It is assumed that if X2 increases that Y will shrink and vice versa. Then the X3 coefficient is negative in the amount of -0.140, it is assumed that if X3 increases that Y will shrink and vice versa.

Table 6 Hypothesis Test Coefficient of Determination Test (R2)

Model	R	R. Square	Adjusted R Square	Std. Error of the Estimate
1	.375 ^a	.141	.089	.56893

Source: Secondary Data Processed by SPSS, 2025

Through Table 6 above, the R square value of the company size, profitability and liquidity variables is 0.141 and explains the earnings quality variable of 14.1%. And the difference (100% - 14.1% = 85.9%) is accompanied by other factors.

Table 7 Model Feasibility Test t

Model		Unstandardized Coefficients		Standardized Coefficients		
		B	Std. Error	Beta	t	Sig.
1	(Constant)	1.889	.331		5.710	.000
	Company Size	.008	.013	.073	.577	.566
	Profitability	-2.873	1.310	-.293	-2.19 3	.033
	Liquidity	-.140	.061	-.301	-2.279	.027
Dependent Variable: Earnings Quality						

Source: Secondary Data Processed by SPSS, 2025

Table 7 shows that X1 has a sig value of 0.566 > 0.05 or it is assumed that X1 does not contribute significantly to Y, Hypothesis 1 is rejected. X2 is worth Sig. 0.033 < 0.05 or it is assumed that X2 contributes significantly to Y, hypotheses 2 is accepted. And X3 is Sig. 0.027 < 0.05 or it is assumed that X3 contributes significantly to Y, hypothesis 3 is accepted.

4. Discussion

The purpose of this study was to analyze the influence of firm size, profitability, and liquidity on earnings quality among manufacturing companies listed on the Indonesia Stock Exchange (IDX) during the 2020–2023 period. Through multiple linear regression analysis, the study has generated several key findings that contribute to both theoretical understanding and practical implications in the field of financial reporting quality.

Firm Size and Earnings Quality

The statistical results show that firm size does not have a significant effect on earnings quality, as indicated by a significance value of 0.566 ($p > 0.05$). This finding suggests that the scale of a company, as measured by total assets or operational magnitude, does not necessarily guarantee better-quality earnings. Although larger firms are typically assumed to have more robust internal control systems, better compliance with regulations, and greater public scrutiny, this study's results challenge that assumption.

One possible explanation lies in the fact that even large firms are not immune to earnings management. High levels of pressure to meet market expectations, sustain stock prices, or justify executive compensation may push even large corporations to manipulate earnings, thereby weakening the expected positive impact of firm size. Furthermore, in the Indonesian context, regulatory enforcement and corporate governance structures may vary in effectiveness, diminishing the supposed benefits of firm size. This finding aligns with prior research (e.g., Solikhah et al., 2022) which argues that firm size alone does not ensure higher reporting transparency unless supported by ethical management behavior and institutional control mechanisms. It also signals that investors and stakeholders should be cautious in assuming that large firms inherently provide more reliable financial information.

Profitability and Earnings Quality

The study finds that profitability has a significant negative influence on earnings quality, as shown by a coefficient of -2.873 and a significance level of 0.033 ($p < 0.05$). This negative relationship may appear counterintuitive at first, as higher profitability is typically associated with financial stability and transparency. However, this result provides empirical evidence that high profitability can also become a motive for earnings manipulation, especially in firms aiming to maintain a consistent trend of financial performance.

Highly profitable companies may face greater market expectations and performance pressure. To maintain their profitability status and meet shareholder demands, management might engage in earnings smoothing or classification shifting—strategies that inflate earnings in the short term but compromise long-term reporting quality. This is consistent with agency theory, which posits that managers, as agents, may prioritize their self-interests (such as bonuses or job security) by manipulating reported earnings, especially when monitoring by principals (investors) is weak. The finding corroborates the insights of Zudana & Opore (2025), who highlight that low transparency and weak external governance may exacerbate the misuse of profitability figures to mislead stakeholders. It also emphasizes the need for improved oversight mechanisms, audit quality, and stronger accounting ethics to ensure that high profitability does not mask underlying financial distortions.

Liquidity and Earnings Quality

Similarly, the variable liquidity is found to have a significant negative effect on earnings quality, with a coefficient of -0.140 and a significance value of 0.027 ($p < 0.05$). This suggests that firms with higher liquidity levels may still report lower-quality earnings. The interpretation of this finding requires a nuanced view of liquidity's role in financial reporting.

Liquidity refers to a company's ability to meet short-term obligations using available cash or liquid assets. While good liquidity is often equated with financial strength and operational efficiency, it can also provide flexibility that enables earnings manipulation. For instance, firms with excess liquidity may engage in transactions or allocate expenditures in a way that benefits short-term earnings appearance rather than reflecting the true economic reality. On the other hand, firms with liquidity constraints may have tighter financial control and less room for discretionary accounting choices. This outcome is supported by studies such as those of Doshchyn (2025) and Fu & Trigilia (2024), which highlight that liquidity abundance does not necessarily prevent opportunistic behavior. Instead, the presence of idle cash can sometimes facilitate more creative accounting practices, particularly in environments with low regulatory scrutiny or weak investor activism.

Model Strength and Statistical Significance

The coefficient of determination (R^2) in this study is 0.141, indicating that only 14.1% of the variation in earnings quality is explained by the three independent variables: firm size, profitability, and liquidity. This relatively low R^2 implies that a large portion (85.9%) of earnings quality is influenced by other factors not captured in this model.

This result underscores the complex and multidimensional nature of earnings quality. Factors such as audit quality, ownership structure, corporate governance mechanisms, accounting policy choices, and industry-specific risks may also play substantial roles in shaping earnings quality. Hence, future research should consider incorporating these additional variables to develop a more comprehensive model of earnings quality determinants.

5. Conclusion

This study sought to investigate the effects of firm size, profitability, and liquidity on earnings quality among manufacturing firms listed on the Indonesia Stock Exchange (IDX) from 2020 to 2023. By applying multiple linear regression analysis, the study provides empirical evidence that profitability and liquidity significantly influence earnings quality, while firm size does not show a significant effect. These findings highlight the critical role of internal financial health indicators—particularly profitability and liquidity—in determining the reliability and sustainability of reported

earnings. From a theoretical perspective, this research reinforces Agency Theory, where managerial decision-making and financial transparency are influenced by the presence (or absence) of effective resource utilization and liquidity management. Companies with higher profitability and stable liquidity tend to reduce agency costs by providing more accurate and credible financial disclosures, mitigating the risk of earnings manipulation.

Practically, this study offers important implications for investors, regulators, and corporate decision-makers. For investors, the results emphasize the importance of looking beyond firm size and focusing on profitability and liquidity as more reliable indicators of earnings quality. For regulators, the study suggests stricter monitoring of earnings reports, especially in firms with poor profitability or liquidity. The findings underline the importance of maintaining robust operational performance and cash flow management for corporate managers to sustain financial credibility. This study urges all financial stakeholders to reassess how earnings quality is interpreted and evaluated in investment and oversight decisions. In an era of increasing corporate complexity and stakeholder scrutiny, earnings quality cannot be solely attributed to firm size or external visibility. Instead, internal financial health—reflected in profitability and liquidity—must become central to financial evaluation frameworks. Additionally, future research is encouraged to expand this analysis by incorporating governance quality, digital financial systems, or industry-specific risk profiles to provide a more holistic view of what drives credible and sustainable financial reporting.

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