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Macroeconomic Determinants: The Mediating Effect of Net Income on Share Price

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Abstract -- *This research focuses on analyzing the impact of exchange rate, interest rate, and inflation on share prices within Indonesia's industrial sector companies listed on the Indonesia Stock Exchange from 2012 to 2024, while excluding the COVID-19 pandemic era (2020-2022). Employing Structural Equation Modeling (SEM) and the Partial Least Squares (PLS) method through SmartPLS 4.0, the study examines five key variables, including net income as a mediating factor between the independent variables (exchange rate, interest rate, inflation) and the dependent variable (share price). The findings reveal that exchange rate volatility has a significant positive influence on net incomes reported by industrial firms. Conversely, interest rates negatively affect net income, suggesting that higher interest charges may hinder financial performance by increasing costs of borrowing. Interestingly, inflation does not significantly impact net income across the surveyed companies, indicating that other factors may mitigate inflation's effects within this context. Furthermore, the study shows that fluctuations in the exchange rate do not directly influence share prices, raising questions about the sensitivity of stock prices to macroeconomic variables in this industrial sector. Nevertheless, net income emerges as a critical determinant positively influencing share prices among the companies analyzed, corroborating the notion that financial performance is closely linked to market valuation. Additionally, the study demonstrates that while net income mediates the relationship between both exchange rate and interest rate with share prices, it does not serve as a mediator in the relationship between inflation and share prices. These results highlight the complexity of financial dynamics within Indonesia's industrial sector and underscore the importance of robust financial performance indicators in shaping market valuations. This research contributes to the broader understanding of investment dynamics in emerging markets, particularly by illuminating the unique interactions between macroeconomic factors and corporate financial health in Indonesia's industrial sector.*

Keywords*: Exchange rate, interest rate, inflation, net income, share price, industrial sector.*

I. INTRODUCTION

In an increasingly interconnected global economy, the interaction between key macroeconomic variables—exchange rates, interest rates, and inflation—plays a pivotal role in shaping corporate performance and stock market valuation (Goodhart et al., 2023). These variables influence corporate profitability, investment decisions, and investor behavior, making them essential determinants of share price dynamics, particularly in emerging markets where financial systems are more sensitive to external shocks (Jia, 2023; Sudarusman et al., 2021; Zahra et al., 2023). Exchange rates affect firms' international competitiveness by altering export prices, import costs, and revenue structures. In Indonesia, fluctuations of the rupiah against major currencies, especially the US dollar, have historically influenced export volumes and corporate earnings. While a depreciating currency may enhance export competitiveness, currency appreciation can suppress foreign demand and reduce profitability (Hatmanu et al., 2020; Jia, 2023; Sudarusman et al., 2021). Although prior studies document a significant relationship between exchange rate movements and stock performance in emerging economies, empirical findings remain inconsistent regarding the direction and magnitude of this effect, indicating the need for further investigation (Annas et al., 2024).

Interest rates represent another fundamental macroeconomic instrument shaping corporate financing behavior and investor preferences (Ahmed & Mazlan, 2021). Rising interest rates increase borrowing costs, potentially constraining capital expenditure and slowing growth, while also encouraging portfolio shifts from equities to fixed-income instruments (Baoquan et al., 2023; Bright-kaitoo & Coffie, 2022). Conversely, accommodative interest rate policies may stimulate investment and consumption, supporting earnings and share prices. However, existing literature reports mixed evidence on whether interest rates exert a direct or indirect

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influence on share prices, suggesting that the transmission mechanism may operate through firm-level financial performance rather than through market valuation alone (Goh et al., 2022).

Inflation further complicates this relationship by eroding purchasing power, increasing production costs, and heightening economic uncertainty. High inflation may weaken consumer demand and compress profit margins, adversely affecting corporate earnings and investor sentiment (Kusumaningtyas et al., 2021; Moyo & Tursoy, 2020). Nevertheless, empirical studies on inflation and stock prices yield divergent results, with some suggesting a negative association and others indicating conditional or insignificant effects (Hatmanu et al., 2020; Jia, 2023; Kar & Jena, 2019). These inconsistencies point to the possibility that inflation influences share prices indirectly through its impact on corporate profitability (Alnaa & Matey, 2022; Mendonça & Lima, 2023).

Despite extensive research on macroeconomic determinants of stock prices, a critical gap persists in the literature (Suriani et al., 2022). Most prior studies examine the direct effects of exchange rates, interest rates, and inflation on share prices, often yielding fragmented and inconclusive findings. Limited attention has been paid to the underlying financial mechanisms through which these macroeconomic variables affect market valuation, particularly the mediating role of net income as a firm-level indicator of financial performance. This omission is especially salient in emerging markets such as Indonesia, where corporate earnings are highly exposed to macroeconomic volatility.

Addressing this gap, the present study positions net income as a central mediating variable linking macroeconomic conditions to share prices (Lwin et al., 2023). Net income encapsulates the cumulative effects of exchange rate movements, interest rate changes, and inflationary pressures on corporate financial health and investor confidence (Bhattacharjee & Das, 2022; Tonkikh et al., 2022). By integrating net income into the analytical framework, this study moves beyond simplistic direct-effect models and offers a more nuanced explanation of how macroeconomic forces translate into stock market outcomes.

The novelty of this research lies in its comprehensive mediation-based approach within the context of Indonesia's industrial sector. Using a longitudinal dataset of publicly listed industrial firms from 2012 to 2024—excluding the COVID-19 pandemic period to avoid extraordinary distortions—and employing Structural Equation Modeling with Partial Least Squares (SEM-PLS), this study simultaneously examines the direct and indirect effects of exchange rates, interest rates, and inflation on share prices through net income. By doing so, it provides robust empirical evidence on the financial transmission mechanism of macroeconomic variables in an emerging market setting.

Ultimately, this study contributes to the literature by clarifying inconsistent empirical findings, enriching theoretical understanding of macro–micro linkages, and offering practical insights for investors and policymakers. It underscores that macroeconomic variables do not operate in isolation, but influence share prices through the financial heartbeat of the firm—net income.

The literature consistently indicates that exchange rates, interest rates, and inflation shape share prices by altering investors' expectations of firms' future performance. Exchange rate movements affect international competitiveness and cost structures: currency appreciation may compress exporters' revenues while lowering import costs for firms reliant on imported inputs, whereas depreciation tends to have the opposite effects. Exchange rates also interact with inflation through import prices and with interest rates through capital flows and portfolio reallocations. Interest rates influence borrowing costs, corporate investment decisions, and household spending. Higher rates typically depress equity valuations by increasing the cost of capital and encouraging substitution toward fixed-income assets, although empirical evidence suggests the magnitude and direction may vary across market contexts. Inflation reduces purchasing power, increases input costs, and heightens uncertainty, often prompting investors to shift toward perceived hedges, thereby increasing equity-market volatility.

Within these transmission mechanisms, net income is widely recognized as a central firm-level indicator that can mediate the effects of macroeconomic conditions on share prices. Earnings that exceed market expectations generally strengthen investor confidence and lift stock valuations, while disappointing earnings trigger sell-offs. However, the earnings–price link is contingent on broader market conditions and perceptions of earnings sustainability.

This study adopts a quantitative research paradigm using secondary data from listed firms' financial statements and macroeconomic indicators (e.g., central bank statistics). Employing regression and/or SEM-PLS, it tests both direct and indirect effects of exchange rates, interest rates, and inflation on share prices, with net income as a mediating variable, to provide empirically robust and policy-relevant insights for investors and decision-makers.

Based on the theoretical study and the explanation above, the researchers proposed a research model according to Figure 1 and developed the following research hypothesis:

Direct effects:
H1: Exchange rate has a significant effect on net income.
H2: Interest rate has a significant effect on net income.
H3: Inflation has a significant effect on net income.
H4: Exchange rate has a significant effect on share price.

H5: Interest rate has a significant effect on share price.
H6: Inflation has a significant effect on share price.
H7: Net income has a significant effect on share price.

Indirect effects (mediation effects):
H8: Net income mediates the relationship between exchange rate and share price.
H9: Net income mediates the relationship between interest rate and share price.
H10: Net income mediates the relationship between inflation and share price.

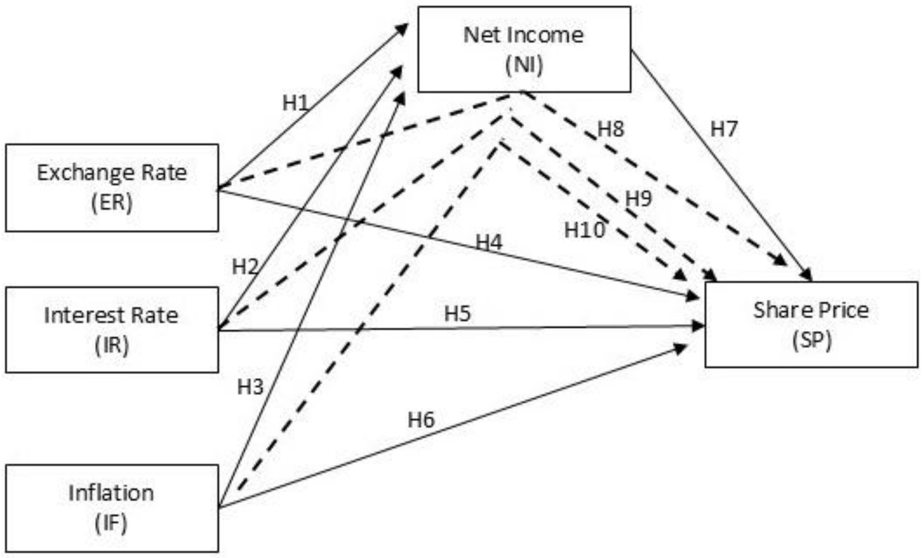

Figure 1. Research Model

II. RESEARCH METHODS

This study employs a quantitative research design to examine the effects of exchange rates, interest rates, and inflation on share prices, with net income as a mediating variable. A quantitative approach is appropriate as it enables objective testing of causal relationships using numerical data and statistical modeling variables (Creswell & Creswell, 2017). The selected macroeconomic variables represent key external forces that influence corporate financial performance and market valuation, particularly in capital-intensive and globally exposed industries.

The study utilizes secondary data from publicly listed companies in the industrial sector of the Indonesia Stock Exchange (IDX), covering the periods 2012–2019 and 2023–2024. The years 2020–2022 are excluded and treated as an anomalous period due to the extraordinary economic disruptions caused by the COVID-19 pandemic, which introduced structural breaks and non-representative financial behavior. This exclusion enhances internal validity and ensures that the analysis reflects normal economic conditions and long-term structural relationships.

The units of analysis are corporate entities, not individual respondents. Using purposive sampling, five industrial-sector companies with the largest asset bases in their respective sub-sectors and complete audited financial data were selected. All sampled firms are listed on the IDX Main Board, ensuring financial transparency, operational maturity, and data reliability. Financial variables—net income and share price—are obtained from audited annual reports, while macroeconomic indicators—exchange rates, interest rates, and inflation—are sourced from Bank Indonesia and the Central Bureau of Statistics (BPS).

Tabel 1. List of Sample Companies

No.	Shares Code	Company Name
1	ASII	PT. Astra International Tbk.
2	UNTR	PT. United Tractors Tbk.
3	MLIA	PT. Mulia Industrindo Tbk
4	HEXA	PT. Hexindo Adiperkasa Tbk.
5	KBLI	PT. KMI Wire & Cable Tbk.

Source: https://www.idx.co.id/en/market-data/stocks-data/stock-list, https://stockbit.com/symbol/AALI/financials (2025)

Volume: 07 No. 01 (2026) https://www.ijosmas.org e-ISSN: 2775-0809

To analyze both direct and indirect relationships, this study applies Structural Equation Modeling using Partial Least Squares (SEM-PLS) with SmartPLS software. SEM-PLS is well suited for financial and macroeconomic research due to its flexibility in handling complex models, mediation effects, non-normal data distributions, and relatively small samples (Hair et al., 2019). The analysis proceeds in two stages: evaluation of the measurement model (indicator reliability, composite reliability, convergent and discriminant validity) and assessment of the structural model (path coefficients, R^2, effect sizes, and predictive relevance) (Bougie & Sekaran, 2019).

Bootstrapping procedures (5,000 resamples) are employed to test the statistical significance of direct, indirect, and mediating effects, allowing for rigorous evaluation of whether net income functions as a full or partial mediator between macroeconomic variables and share prices. Multicollinearity is assessed using Variance Inflation Factors (VIF), while model quality is further evaluated through R^2, f^2, and Q^2 statistics.

Although PLS-SEM does not require strict classical assumptions, complementary diagnostics such as normality and heteroskedasticity tests may be conducted to enhance robustness. Overall, this methodological framework ensures analytical rigor, reliability, and explanatory depth, enabling the study to generate empirically sound insights into how macroeconomic conditions influence corporate valuation through financial performance in Indonesia’s industrial sector.

III. RESULTS AND DISCUSSION

Results

This section synthesizes the empirical findings for ten hypotheses (H1–H10) examining how exchange rates, interest rates, and inflation affect net income and share prices in Indonesia’s industrial sector, including the mediating role of net income. Overall, the findings reinforce the view that macroeconomic shocks matter, but their influence is often transmitted through firm profitability and sector-specific resilience rather than direct pricing effects in the stock market.

H1: Exchange Rate → Net Income (Positive and Significant)

The results indicate that exchange rate fluctuations positively affect net income for industrial firms listed on the IDX. This finding challenges the conventional expectation that currency volatility uniformly harms corporate performance in emerging markets. In the Indonesian context, rupiah depreciation can improve export competitiveness and enlarge export revenues when translated into rupiah, thereby strengthening net income—especially for industrial firms with meaningful foreign-market exposure. The result is consistent with evidence suggesting depreciation can stimulate export volumes and support industrial profitability. Importantly, the finding also implies that exchange rate risk is not merely a threat but can become a strategic advantage when firms are positioned to benefit from external demand and currency translation gains.

A key interpretive mechanism is firms’ adaptive capacity, including hedging and operational strategies that reduce downside risk while preserving upside potential. The results suggest that industrial firms may be better equipped than other sectors to manage currency exposure through risk management practices, diversified sourcing, and contractual arrangements. Hence, exchange rate movements appear to function as an opportunity structure for industrial net income under certain market configurations, rather than a purely destabilizing force.

H2: Interest Rate → Net Income (Negative and Significant)

The findings show a significant inverse relationship between interest rates and net income. When interest rates rise, industrial firms face higher financing costs, which compress profitability—particularly in capital-intensive businesses that rely on debt to support operations and expansion. This result aligns strongly with standard monetary transmission theory: higher borrowing costs discourage investment, constrain working capital, and may weaken demand through reduced consumer purchasing power. The analysis further implies that interest-rate sensitivity is heightened in sectors with high leverage and long investment horizons, where interest expenses can materially reshape income statements.

From a managerial perspective, the evidence supports the strategic relevance of interest rate risk management, including refinancing strategies, fixed-rate debt structures, and operational efficiency programs to offset rising costs. From a policy angle, the results underscore that interest-rate adjustments may influence corporate profitability even when share prices do not respond directly.

H3: Inflation → Net Income (Not Significant)

The study finds that inflation does not significantly affect net income within the sample of industrial firms. This suggests that industrial companies may have stronger capabilities to buffer inflation through pricing strategies, cost controls, productivity improvements, and input substitutions. In some periods, inflation even correlates positively with net income, implying that certain firms may pass cost increases to customers without substantial demand erosion, or benefit from nominal revenue increases that outpace cost escalation.

This outcome also resonates with the idea that reported earnings may reflect income smoothing or managerial adjustments that stabilize profitability under inflationary pressure. The key implication is that inflation may not automatically translate into net income deterioration in industrial firms—particularly when market structures allow for partial pass-through and when firms possess scale and bargaining power.

H4: Exchange Rate → Share Price (Not Significant)

The results show that exchange rate fluctuations do not have a statistically significant direct effect on share prices. While exchange rate changes influence firm profitability (as supported in H1), the market may not price currency movements directly into share prices, possibly because investors interpret currency shocks as transitory, or because hedging and operational buffers reduce the perceived earnings risk. This suggests that, in this sector and period, investors may rely more heavily on firm fundamentals (profitability, governance, strategic execution) than on exchange rate indicators alone.

This finding also indicates that the share-price formation process in Indonesia's industrial sector may be driven more by internal corporate performance and domestic market sentiment than by currency movements per se. It invites a recalibration of investor analysis: exchange rates remain important, but primarily as inputs affecting profitability rather than as stand-alone predictors of stock valuation.

H5: Net Income → Share Price (Positive and Significant)

Consistent with valuation logic and market behavior, net income positively and significantly affects share prices. Investors appear to reward firms exhibiting stronger profitability, interpreting net income as a credible signal of operational strength, growth capacity, and dividend potential. This finding aligns with a wide body of evidence that earnings performance is central to stock valuation, particularly in sectors where cash generation and profitability are primary indicators of resilience.

However, the result also implies that the earnings signal is interpreted within broader contexts: market conditions, sustainability of profit drivers, and credibility of reporting practices can amplify or moderate the market response. Nevertheless, within this sample, net income remains the most reliable proximate determinant of share price.

H6: Inflation → Share Price (Not Significant)

The findings indicate that inflation does not significantly influence share prices for industrial firms over the study horizon. This suggests that investors either anticipate and absorb inflation into expectations, or consider inflation effects to be already reflected via monetary policy, sector pricing power, and firm-level strategies. It may also imply that inflation during the sampled periods did not reach levels that triggered broad equity repricing, or that industrial firms are perceived as relatively insulated due to demand stability and scale.

This reinforces a key point: macroeconomic variables can have context-dependent pricing power in capital markets. Inflation may matter in some sectors or periods, but in the Indonesian industrial sector during 2012–2019 and 2023–2024, it does not appear to be a decisive pricing factor.

H7: Interest Rate → Share Price (Not Significant)

Interestingly, interest rate changes do not significantly affect share prices, even though interest rates significantly affect net income (H2). This pattern suggests that the market's interest-rate channel may be indirect and possibly dominated by firm fundamentals and investor sentiment. It is also plausible that investors focus on profitability and firm strategy as the core valuation anchors, while interest rate impacts are perceived as manageable, already anticipated, or offset by other macro conditions. This result supports the notion that in emerging markets and sector-specific settings, share prices may be less responsive to single macro indicators and more responsive to internal financial performance metrics.

H8: Mediation—Exchange Rate → Net Income → Share Price (Supported)

Given that exchange rates significantly increase net income (H1) and net income significantly increases share price (H5), the results support the conclusion that net income mediates the relationship between exchange rates and share prices. This mechanism clarifies why exchange rates show no direct effect on share prices (H4): currency movements matter insofar as they translate into earnings performance. The market appears to respond primarily to what exchange rate changes do to profitability, rather than to the exchange rate itself.

H9: Mediation—Interest Rate → Net Income → Share Price (Supported)

Similarly, the evidence suggests net income mediates the relationship between interest rates and share prices. Rising interest rates reduce net income (H2), which in turn affects share prices (H5). This explains the non-significant direct interest-rate effect on share prices (H7): the market reacts more strongly to the profitability outcomes of interest rate changes than to rate changes as isolated information.

H10: Mediation—Inflation → Net Income → Share Price (Not Supported)

Volume: 07 No. 01 (2026) https://www.ijosmas.org e-ISSN: 2775-0809

Finally, the results indicate that net income does not mediate the relationship between inflation and share prices. This is consistent with inflation being non-significant for net income (H3) and also non-significant for share prices (H6). The implication is that, within this sector and timeframe, inflation does not meaningfully transmit into firm profitability or market valuation through the net income channel, suggesting that other pathways—if any—would likely involve sentiment, policy expectations, or sector demand dynamics rather than earnings mediation.

Collectively, the findings highlight a coherent structural story: net income is the dominant transmission mechanism through which macroeconomic forces (especially exchange rates and interest rates) influence share prices. Inflation, in contrast, appears muted in both profitability and valuation for the industrial firms examined. For investors, this supports a strategy centered on earnings quality, profitability resilience, and managerial capability, while treating macro indicators as contextual drivers that operate primarily through financial performance. For policymakers, the results imply that monetary shifts—especially interest-rate policy—may affect corporate profitability even when equity prices do not respond immediately, emphasizing the importance of stability and predictability in macro-financial governance.

Discussion

The findings collectively suggest that macroeconomic variables shape share price dynamics in Indonesia's industrial sector primarily through profitability transmission, rather than through direct market repricing of macro indicators. Two patterns are particularly salient. First, exchange rate movements significantly improve net income (H1), consistent with an export-competitiveness and currency-translation mechanism in which rupiah depreciation increases export revenues in domestic currency terms. This outcome also implies that industrial firms possess relatively strong adaptive capacity—through hedging, procurement strategies, and operational adjustments—enabling them to convert exchange-rate volatility into performance gains rather than earnings disruption (Badhan, 2024; Mesagan et al., 2021). Yet, exchange rates show no direct effect on share prices (H4), indicating that investors may treat exchange-rate shocks as indirect information that becomes valuation-relevant only once reflected in firm earnings (Napitupulu et al., 2024).

Second, interest rates exhibit a clear negative impact on net income (H2), consistent with the cost-of-capital channel and the sensitivity of capital-intensive industrial firms to borrowing costs (Basmar et al., 2019; Jahidah et al., 2024). However, interest rates do not significantly affect share prices directly (H7). This divergence reinforces the interpretation that the market's pricing mechanism relies more heavily on firm fundamentals—particularly realized profitability—than on macro indicators in isolation (Halim et al., 2022). In this regard, net income emerges as the key valuation anchor, evidenced by its strong positive influence on share prices (H5). This aligns with valuation theory and the informational role of accounting earnings in guiding investor expectations (Choiriyah et al., 2021).

Inflation is non-significant for both net income (H3) and share prices (H6), suggesting that industrial firms may effectively manage inflation pressures via pricing power, cost control, productivity improvements, or contractual arrangements that stabilize margins (Hasmirati & Akuba, 2022). It also implies that inflation within the study window may have been largely anticipated and absorbed by market participants, limiting incremental informational content (Kumar, 2024).

Importantly, mediation tests confirm that net income mediates the effects of exchange rates (H8) and interest rates (H9) on share prices, but not inflation (H10). Practically, these results direct investors toward monitoring macro variables insofar as they affect profitability trajectories, while firms should prioritize risk management and operational resilience to stabilize net income under macroeconomic volatility (Fatmayuni et al., 2024; Rocha et al., 2018).

IV. CONCLUSION

This study concludes that macroeconomic variables influence corporate valuation in Indonesia's industrial sector primarily through firm profitability, rather than through direct stock market reactions. Exchange rates and interest rates significantly affect net income, while inflation shows no significant impact on either net income or share prices during the observed period (2012–2024, excluding COVID-19 years). Exchange rate movements, particularly currency depreciation, can enhance industrial firms' profitability through export competitiveness, whereas rising interest rates tend to suppress net income by increasing financing costs. In contrast, inflation appears to be effectively absorbed through pricing strategies and operational adjustments. Importantly, net income significantly drives share prices, confirming profitability as the dominant valuation signal for investors. Accordingly, net income mediates the effects of exchange rates and interest rates on share prices, but does not mediate the inflation–share price relationship.

Theoretical implications lie in strengthening the financial transmission perspective: macroeconomic shocks do not affect equity prices mechanically, but operate through internal performance metrics—especially earnings. By positioning net income as a mediating variable, this study refines asset pricing insights for emerging markets and contextualizes global macro-finance theories within Indonesia's industrial landscape.

Practical implications are threefold. Corporate managers should prioritize profitability resilience via cost efficiency, revenue diversification, and risk management (e.g., hedging and debt structure optimization). Investors should anchor decisions on earnings quality and sustainability, using macro indicators to interpret—not replace—firm fundamentals. Policymakers should calibrate monetary actions mindful of their indirect effects on corporate earnings and capital markets.

Limitations include sectoral focus (industrials), country specificity (Indonesia), and omission of factors such as political risk, commodity prices, and investor sentiment. Methodologically, SEM-PLS, while robust, cannot fully capture market complexity or establish strict causality.

Recommendations encourage future research to extend across sectors and countries, adopt longitudinal designs, and integrate additional macro-financial variables. Practically, advancing managerial financial literacy and macroeconomic awareness will further enhance corporate adaptability and market stability in volatile environments.

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