The Impacts of Free Cash Flow and Agency Cost on Firm Performance

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ARTICLE INFO	ABSTRACT
	This study aims to examine the effect of free cash flow and agency cost to firm performance. The purpose of this study to provide empirically evidence about the effect of free cash flow and agency cost to firm performance. This study also examines the free cash flow hypothesis. Recent study about this topic resulting mixed/various result. Free cash flow in this study measured by free cash flow t-1, agency cost proxied by operating expenses ratio. Firm performance divided into three, operational performance measured by ROA, firm value measured by tobin's q ratio, and share return measured by holding period return. This study will conduct on manufacturing companies listed on Indonesian Stock Exchange period of 2017-2021. Sample were selected by purposive random sampling method and finally obtained 396 samples that fulfill the criteria. Data were analyzed using multiple regression analysis. The result show that free cash flow has insignificant positive effect on firm operational performance, firm value and share return. Agency cost has significant negative effect on firm operational performance, firm value and share return. This study provides empirical evidence of the effect agency cost on firm performance and provides contribution to the literature on free cash flow hypothesis topics. Keywords: Agency Cost, Free Cash Flow, Holding Period Return, Return On Asset.

INTRODUCTION

The main purpose of the company in doing business is to develop growth of the company (Wang, 2010). Another purpose is also to maximizing shareholder wealth with increase the value of the firm (Purnawarman & Handayati, 2021). This objective pursued by managing assets and resources owned by the firm in order to obtain profit for the firm. Investment is one of important factor in the growth of the company (Giriati, 2016).

Company is a set of contracts between owners (principals) and managers (agents) (Jensen & Meckling, 1976). The manager (agent) working for the shareholder interest (principal). In reality, each stakeholder has their own interests, shareholders interest is to maximize their wealth through

dividend payments, while management interest is to growth the firm size that will have an impact on promotion and compensation to management (Purnawarman and Handayati, 2021).

When shareholders and managers have different interests, conflicts of interest or agency problems have occurred between shareholders and management, so there is the potential for companies to be managed by management for their personal interests. To overcome this, shareholders create monitoring devices to force manager acts and make decision for shareholder interests, not for personal interest (Purnawarman and Handayati, 2021). Agency costs are costs incurred as a result of making supervisory devices to reduce the potential for agency problems to occur (Jensen and Meckling, 1976).

Shareholder have an interest in increasing their wealth from free cash flow distribution through dividends, while managers have an interest in using free cash flow to expand the company (Purnawarman and Handayati, 2021). Free cash flow is net cash flow minus the firm's investment funding needs. Large amounts of free cash flow that generate by companies can raise agency problems potential between management and shareholder (Sapuan, 2021). Manager of the firm tends to allocate the amount of free cash flow for unprofitable uses. This is not in line with the shareholder interest to maximizing their wealth by increasing the shares value or dividend payments (Almeida et al., 2004).

Theory of free cash flow hypothesis developed by Jensen, (1986) explains that an increase in free cash flow will be followed by an increase in the intention of manager to waste free cash flow by making bad investment decisions that result in company performance (Fosberg & Rosenberg, 2003). The ineffective and inefficient use of free cash flow will increase agency costs. Increases and decreases in agency costs contribute to firm performance where there is a decrease in costs, it will increase firm performance (Fauziyah & Kustinah, 2023).

Previous research about effect of free cash flow (FCF) and agency cost on firm performance obtained mixed findings (Chen et al., 2016). Purnawarman and Handayati (2021) and Piramita, (2021) found that a firm financial performance is positively influenced by free cash flow, as well as Wang (2010) and Lachheb & Slim, (2017) found that free cash flow (FCF) has a positive impact on a firm performance. The opposite result conducted by Richardson, (2006), Yuan & Jiang, (2008) which found that free cash flow is positively related to overinvestment, which means that the greater the free cash flow, the greater the overinvestment, which means the lower the firm performance (Zhang, 2016). The results of Pacheco, (2018) also found that free cash flow has a negative effect on firm value which is proxied by Tobin's Q Ratio. Andini & Wirawati, (2014) also found that free cash flow has a negative and significant effect on company financial performance. This is in line with Jensen's (1986) free cash flow hypothesis.

Previous studies result that are still mixed are the reasons to conduct this research. This study also re-examines the free cash flow hypothesis proposed by Jensen (1986). This research is expected to provide additional empirical evidence of the relationship between free cash flow (FCF), agency costs and firm performance in Indonesia.

LITERATURE REVIEW AND HYPOTHESIS DEVELOPMENT
Agency Theory
Jensen and Meckling (1976) describe agency as a principal-agent relationship in which the principal employs an agent to perform work related to the principal's interests (Chu, 2011). The separate ownership and management functions in a company contain the potential for agency conflicts or problems (Jensen and Meckling, 1976). Human nature that prioritizing personal interest is the reason why manger not act for shareholder interest. When manager (agent) prioritized their personal interest above the shareholder interest that trigger agency problem. Generally, agency problem will cost shareholder as a principal (Brush et al., 2000).

Free cash flow that owned by the firm related to agency problem (Jensen and Meckling, 1976). Free cash flow is net cash flow minus the company's investment funding needs. Shareholder and manager have different interest on firm free cash flow (Budiardi, 2019). shareholder wants to get return from dividend payment, but manager prefer to expand the firm for increasing firm growth that will increase their compensations or bonuses (Singh & Davidson III, 2003).

Increasing free cash flow followed by increasing manager intention to waste free cash flow with bad investment decisions and inefficiency cost for personal interest. Shareholders must create monitoring devices to control and forces manager to act based on principal interest. The cost that caused by creating monitoring devices to minimize agency problem is agency cost (Jensen and Meckling, 1976).

Research Framework
This study empirically tested the effect of free cash flow and agency cost on firm performance. Size and leverage used in this study as control variables. Therefore formed research framework as follows:
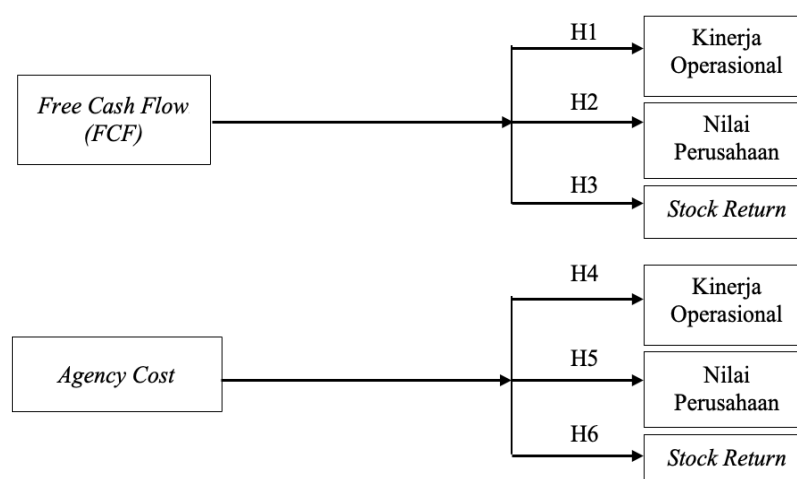

Figure 1. Research Framework
Source: primary data

Free cash flow and firm performance
Free cash flows hypothesis and the agency theory explained that free cash flows had a negative impact on firm performance (Khidmat & Rehman, 2014). The large amount of free cash flow will make managers tend to invest in projects that have a low probability of success with a bad NPV which makes the firm performance decrease (Yusuf et al., 2018). Declining firm performance will also reduce the value of the firm. This study divide firm performance into operating performance, firm value and stock return. Therefore formed the hypothesis:
H1: Free cash flow (FCF) have a negative impact on operating performance.
H2: Free cash flows have a negative impact on firm value.
H3: Free cash flows have a negative impact on stock return.

Agency cost and firm performance
Based on agency theory, conflict of interest potential in agency problems force shareholders to create a device to supervise and control management so that they act and make decisions in term of maximizing the wealth of the shareholders. The costs arising from agency problem potential

classified as agency cost (Jensen and Meckling, 1976). Agency cost is an expense that reduce firm profit that can decrease firm performance. This study divides firm performance into operating performance, firm value and stock return. Therefore formed the hypothesis:

H4: Agency costs have a negative impact on operating performance.
H5: Agency costs have a negative impact on firm value.
H6: Agency costs have a negative impact on stock return.

METHODS

Sample selection and data collection
This study conducted on listed manufacturing companies in Indonesia Stock Exchange period of 2017-2021. Manufacturing companies are the most companies in Indonesian Stock Exchange. Manufacturing companies also consist of almost all sector on Indonesian Stock Exchange (Njauwman, 2021).

The Sample selection was carried out using certain criteria. Those criteria are the company had positive equity; using IDR in financial report; had positive equity; and have all required research variable data. Data will be collected from financial report, annual report and website of the company. Finally obtained 396 observation sample.

Analysis methodology
This research tries to empirically test the effect of free cash flow (FCF) and agency costs on firm performance. Analysis will conduct using multiple regression analysis. The classical assumption also tested the regression model to make sure obtained the best model in term of estimation, unbiased and consistent.

Research model and variables measurement
Firm performance divide into three indicator, operating performance, firm value and stock return. Operating Performance proxied by Return on Asset (ROA). Firm Value proxied by Tobin's Q Ratio. Stock Return Proxied by Holding Period Return (HPR). The calculation of the firm performance proxies define as follows:

$$ROA_t = \frac{\text{Laba bersih}_t}{\frac{1}{2}(\text{Aset}_{t-1} + \text{Aset}_t)}$$

where ROA denotes Return on Asset, NI denotes Net Income, Asset denotes Total Asset.

$$Q_t = \frac{Market\ Value\ of\ Stock_t + Total\ Debt_t}{Total\ Asset_t}$$

where Q denotes Tobin's Q Ratio, MVS denotes Market Value of Stock, Debt denotes Total Debt.

$$HPR_t = \frac{Stock\ Price_t - Stock\ Price_{t-1}}{Stock\ Price_{t-1}}$$

where HPR denotes Holding Period Return.

Free cash flow using in this research is the calculation used by Gul (2001), Wang (2010), Lachheb and Slim (2017). The calculation of free cash flow expressed as follows:

$$FCF_t = \frac{OCF_t - CDiv_t}{Sales_t}$$

where OCF denotes Operating Cash Flows, CDiv denotes Cash Dividends, Sales denotes Net Sales. Based on literature, agency cost measurement is still not clearly defined. this research use operating expenses ratio to total asset used by Wang (2010) and Lachheb and Slim (2017) to measured agency cost. Operating expenses ratio defined as follows:

$$OER_t = \frac{OE_t}{Asset_t}$$

Where OER denotes Operating Expenses Ratio, OE denotes Operating Expenses and Asset denotes total asset.

Size and leverage also used in this study as control variable. Literature said that size and leverage are included to four commonly used to control their influences to dependent variables (Wang, 2010).

$$Size = Ln\ (Total\ Asset)$$

$$DTA = \frac{Total\ Debt}{Total\ Asset}$$

where DTA denotes leverage.

This research tries to empirically test the effect of free cash flow (FCF) and agency cost on firm performance. To explore how free cash flows and agency costs impact on the operational performance we used the following regression models:

$$ROA_t = \alpha\ +\ \beta_1\ FCF_{t-1} +\ \beta_2\ OER_t + \beta_3\ Size_t + \beta_4\ DTA_t + e \qquad (1)$$

to explore how free cash flows and agency costs impact on the firm value we used the following regression models:

$$Q_t = \alpha\ +\ \beta_1\ FCF_{t-1} +\ \beta_2\ OER_t + \beta_3\ Size_t + \beta_4\ DTA_t + e \quad (2)$$

to explore how free cash flows and agency costs impact on the stock return we used the following regression models:

$$Ri = \alpha\ +\ \beta_1\ FCF_{t-1} +\ \beta_2\ OER_t + \beta_3\ Size_t + \beta_4\ DTA_t + e \quad (3)$$

RESULTS AND DISCUSSION

Descriptive Statistic
Descriptive statistical analysis was carried out to get an overview of the data by analyzing the value of the mean, minimum, maximum and standard deviation values for each variable. Descriptive statistical analysis was performed on all variables used in this study using eviews 12. Table 1 show the result of descriptive statistical analysis.

Table 1. Statistic Descriptive Analysis

	Mean	Maximum	Minimum	Std. Dev.	Observation
FCF	0,050394	1,222509	-1,785064	0,143775	396
OER	0,961230	3,285039	0,555891	0,273037	396
ROA	0,045032	0,253153	-0,181032	0,069317	396
TOBINS_Q	1,446571	6,436595	0,359695	0,945713	396
HPR	0,000972	1,253425	-0,821429	0,314403	396
SIZE	28,586350	32,819920	25,689500	1,532149	396
LEVERAGE	0,430644	0,931277	0,063029	0,198558	396

Source: SPSS processing results

Classical Assumption Test

The classical assumption tested to ensure the regression model obtained the best model in term of estimation, unbiased and consistent. The model in this research tested by multicollinearity test, autocorrelation test and heteroscedasticity test.

Table 2. report the Variance Inflation Factors (VIF) score of the regression model. VIF score used to detect multicollinearity. If VIF score ≥ 10 that means there are multicollinearity in the regression model. The good regression model is the model that doesn't have multicollinearity. VIF score from table 2. show that all variable on all regression model does not have multicollinearity problem.

Table 2. VIF Score

Variabel	1 (ROA) VIF	2 (Q) VIF	3 (Ri) VIF
C			
FCF	1,037989	1,037989	1,037989
OER	1,035952	1,035952	1,035952
SIZE	1,067415	1,067415	1,067415
LEVERAGE	1,054532	1,054532	1,054532

Source: SPSS processing results

Autocorrelation test was carried out with Durbin Watson value. In the Durbin Watson autocorrelation test, the conditions used are that the regression model does not have autocorrelation if $2 < d < 4$; $du < d < 2$; $du < d < 4-du$. d denotes for Durbin Watson value, du value is taken from Durbin Watson Table.

Table 3. Durbin Watson

Model Regresi	DW	du	dl
1 (ROA)	2,287168	1, 84933	1,81834
2 (TOBINS_Q)	2,159405	1, 84933	1,81834
3 (Ri)	1,885660	1, 84933	1,81834

Source: SPSS processing results

Table 3. shows that are no autocorrelation occurs on all regression models.

The heteroscedasticity test used the Glejser test. The Glejser test suggests to analysis regression of the residual absolute value to independent variable (Gujarati & Porter., 2009). If the independent variable has a significant relationship with the residual absolute value, then there is an indication of heteroscedasticity. A model that does not have heteroscedasticity is a good regression model, when the variance of the residual from one observation to another is fixed (homoscedasticity) (Ghozali, 2012).

Table 4. Glejser test

Variabel	1 (ROA) Sig.	2 (Q) Sig.	3 (Ri) Sig.
C	0,233800	0,041000	0,000100
FCF	0,041000	0,607100	0,749400
OER	0,000000	0,009600	0,290500

SIZE	0,609900	0,000000	0,004800
LEVERAGE	0,000100	0,000000	0,037400

Source: SPSS processing results

Table 4. shows the result of the heteroscedasticity test and shows that there are heteroscedasticity problem on all regression models in this study.

F-Test
F-test was conducted to find out whether the independent variables simultaneously affect dependent variables. F-test result can be drawn from table 5.

Table 5. Multiple Regression Analysis

Model Regresi	R^2	*Adjusted R^2*	Prob (F-Statistic)
1 (ROA)*	0,370692	0,364254	0,000000
2 (TOBINS_Q)*	0,085164	0,075805	0,000000
3 (Ri)*	0,037259	0,027410	0,004900

*dilakukan analisis regresi menggunakan *Robust Standard Error (Huber-White)*
Source: SPSS processing results

Table 5. shows result of f-test for all of three regression model used in this study. First regression model using return on asset (ROA) as dependent variable. Second regression model using tobin's q ratio (TOBINS_Q) as dependent variable. Third regression model using holding period return (Ri) as dependent variable.

Result for first regression model on table 5. shows Prob (F-Statistic) or significance value 0,000000 (<0,05). That result means all the independent variables in first model (FCF, OER, Size, Leverage) affect dependent variable (ROA) simultaneously.

Result for second regression model on table 5. shows Prob (F-Statistic) or significance value 0,000000 (<0,05). That result means all the independent variables in first model (FCF, OER, Size, Leverage) affect dependent variable (TOBINS_Q) simultaneously.

Result for third regression model on table 5. shows Prob (F-Statistic) or significance value 0,004900 (<0,05). That result means all the independent variables in first model (FCF, OER, Size, Leverage) affect dependent variable (Ri) simultaneously.

Coefficient determination
Coefficient determination was conduct using Adjusted R^2 to find how much independent variables simultaneously affect the dependent variables. Table 5. shows value of adjusted R^2 for all of three regression model used in this study. First regression model using return on asset (ROA) as dependent variable. Dependent variable for second regression model is tobin's q ratio (TOBINS_Q). Third regression model using holding period return (Ri) as dependent variable.

Result for first regression model on table 5. shows Adjusted R^2 value 0,364254. That result means the dependent variable (ROA) determined by all the independent variables in the first regression model (FCF, OER, Size, Leverage) by 36,42%.

Result for second regression model on table 5. shows Adjusted R^2 value 0,075805. That result means the dependent variable (TOBINS_Q) determined by all the independent variables in the second regression model (FCF, OER, Size, Leverage) by 7,58%.

Result for third regression model on table 5. shows Adjusted R^2 value 0,027410. That result means the dependent variable (Ri) determined by all the independent variables in the third regression model (FCF, OER, Size, Leverage) by 2,74%.

Hypothesis test (t-test)
a. T-test

Test of t-statistical was conducted to find out how much the dependent variable affected by the independent variable individually (Ghozali, 2012). Regression model run and analysis using multiple regression with robust standard error (Huber-White) to make sure the model robust from autocorrelation and heteroscedasticity problem. T-test result can be drawn from table 6.

Table 6. First Regression Model t Statistical Test

Var.Dep	(1) ROA*		(2) TOBINS_Q*		(3) Ri*	
Var.Ind	**Coefficient**	**Sig.**	**Coefficient**	**Sig.**	**Coefficient**	**Sig.**
C	-0,120246	0,033900	-1,673641	0,046100	0,591568	0,028400
FCF	0,030859	0,232700	0,147807	0,652000	0,127762	0,242100
OER	-0,086383	0,000000	-0,545648	0,002300	-0,112623	0,006800
SIZE	0,011090	0,000000	0,138869	0,000000	-0,01459	0,127900
LEVERAGE	-0,163139	0,000000	-0,772117	0,002000	-0,166514	0,048300

*dilakukan analisis regresi menggunakan *Robust Standard Error (Huber-White)*
Source: SPSS processing results

Table 6. shows the result of t statistic test for H1 and H4. From these results it can be interpreted that the first regression model with the dependent variable proxied using ROA, a significance value of 0.232700 is obtained with a positive coefficient on the FCF independent variable. This means that the free cash flow variable has no significant positive effect on ROA as proxies of operating performance. These results do not support the first hypothesis (H1), which is also not in line with the theory of the free cash flow hypothesis developed by Jensen (1986).

Table 6. on first regression model also shows the result for H4. Result shows that significance value of OER is 0,000000 with negative coefficient value. That means agency cost (OER) has a significant negative effect on operating performance (ROA). These results support the fourth hypothesis (H4), which is also in line with the theory of the free cash flow hypothesis developed by Jensen (1986).

Table 6. also shows the result of t statistic test for H2 and H5 from second regression model. From these results it can be interpreted that the second regression model with the dependent variable proxied using tobin's q Ratio, a significance value of 0.652000 is obtained with a positive coefficient on the FCF independent variable. This means that the free cash flow variable has no significant positive effect on tobin's q ratio as proxies of firm value. These results do not support the second hypothesis (H2), which is also not in line with the theory of the free cash flow hypothesis developed by Jensen (1986).

Table 6. on second regression model also shows the result for H5. Result shows that significance value of OER is 0,002300 with negative coefficient value. That means agency cost (OER) has a significant negative effect on firm value (tobin's q ratio). These results support the fifth hypothesis (H5), which is also in line with the theory of the free cash flow hypothesis developed by Jensen (1986).

Table 6. also shows the result of t statistic test for H3 and H6 from third regression model. From these results it can be interpreted that the third regression model with the dependent variable proxied using holding period return, a significance value of 0.242100 is obtained with a positive coefficient on the FCF independent variable. This means that the free cash flow variable has no significant positive effect on holding period return as proxies of share return. These results do not support the third hypothesis (H3), which is also not in line with the theory of the free cash flow hypothesis developed by Jensen (1986).

Table 6. on third regression model also shows the result for H6. Result shows that significance value of OER is 0,006800 with negative coefficient value. That means agency cost (OER) has a significant negative effect on share return (holding period return). These results support the sixth hypothesis (H6), which is also in line with the theory of the free cash flow hypothesis developed by Jensen (1986).

b. Path Analysis

Hypothesis testing is done by testing two values, namely the p-value is smaller than the alpha value of 5% (<0.05) and the t-statistic value must have a value greater than 1.96 (<1.96). The results of the calculation of the significance of each relationship between variables are presented in Table 7.

Table 7 Test of Direct Influence of Variables

Pengaruh Langsung	Path Coefficient	T Statistics	P Values	Keterangan
Free Cash Flow -> Operating Performance	0.165	0.232700	0.329	Tidak Signifikan
Free Cash Flow -> Firm Value	0.218	0.652000	0.302	Tidak Signifikan
Free Cash Flow -> Stock Return	0.617	0.242100	0.089	Tidak Signifikan
Agency Cost -> Operating Performance	0.048	0.000000	0.582	Signifikan
Agency Cost -> Firm Value	0.526	0.000000	0. 363	Signifikan
Agency Cost -> Stock Return	0.476	0.000000	0.187	Signifikan

Source: SPSS processing results

Based on table 7, the results of the direct effect between variables are as follows:
1) Free Cash Flow Have a Negative Impact on Operating Performance
   Based on the test results, the path coefficient value is 0.165 with a t-statistic value of 0.232700 and a p-value of 0.329. This means that H1 is rejected and there is a negative and insignificant influence between Free Cash Flow and Operating Performance.
2) Free Cash Flow Have a Negative Impact on Firm Value
   Based on the test results, the path coefficient value is 0.218 with a t-statistic value of 0.652000 and a p-value of 0.302. This means that H2 is rejected and there is a negative and insignificant influence between Free Cash Flow and Firm Value.

3) Free Cash Flow Have a Negative Impact on Stock Return
Based on the test results, the path coefficient value is 0.617 with a t-statistic value of 0.242100 and a p-value of 0.089. This means that H3 is rejected and insignificant between Free Cash Flow and Stock Return.
4) Agency Cost Have a Negative Impact on Operating Performance
Based on the test results, the path coefficient value is 0.048 with a t-statistic value of 0.00000 and a p-value of 0.582. This means that H4 is rejected and there is a negative and significant influence between Agency Cost and Operating Performance.
5) Agency Cost Have a Negative Impact on Firm Value
Based on the test results, the path coefficient value is 0.526 with a t-statistic value of 0.00000 and a p-value of 0.363. This means that H4 is rejected and there is a negative and significant influence between Agency Cost and Firm Value.
6) Agency Cost Have a Negative Impact on Stock Return
Based on the test results, the path coefficient value is 0.476 with a t-statistic value of 0.00000 and a p-value of 0.187. This means that H4 is rejected and there is a negative and significant influence between Agency Cost and Stock Return.

Free Cash Flow Impact on Operating Performance
The results showed that Free Cash Flow has no effect on Operating Performance. So that H1 is rejected. The existence of a large Free Cash Flow illustrates that the company is able to manage cash well, so that large cash is used to make investments by purchasing fixed assets or purchasing shares, making acquisitions or new innovations related to products within the company (Jaya, 2020). If the company has high free cash flow, the company has good performance compared to companies that have free cash flow. A company that generates excess value from free cash flow and does not have profitable investment opportunities, management will deviate from the results of existing free cash flow, causing an increase in agency costs and inefficient resource allocation. In addition, the wrong investment will result in decreased financial performance . It is also supported by research conducted by Mursidah, (2021) which states that the higher the level of free cash flow, the company's financial performance will improve so that it has a good impact on company profitability. Different from Komarudin et al., (2019) which states that free cash flow affects company performance but is not significant.

Free Cash Flow Impact on Firm Value
The results showed that Free Cash Flow has no effect on Operating Performance. So that H2 is rejected. This result is possible because of several possibilities, including free cash flow is not always used in activities that directly affect the company's operational performance, high corporate debt gives the company an obligation to pay debts which makes free cash flow insufficient for investment and operational performance improvement, precautionary management policies that retain free cash flow rather than invest it.

Free cash flow is also the result of firm historical performance. firm value and share return is calculated using share price that influenced by many factors related to investors expectations of the firm in the future. This is what might make the relationship between free cash flow, firm value and share return insignificant (Septrinova & Edi, 2021).

The results of this study are also supported by Zurriah, (2021) which states that the free cash flow variable simultaneously and partially has a positive and significant effectt on firm value. This cash flow reflects the rate of return for investors, be it in the form of debt or equity. Free cash flow can be used to pay debt, buy back shares, pay dividends or be saved for future growth opportunities. If the free cash flow of the company is positive (FCF $\geq$ 0) then the company's finances are in good condition while if the free cash flow of the company is negative (FCF $\leq$ 0) and the company must issue shares for capital increase, it will result in reduced profits per share of the company.

Free Cash Flow Impact on Stock Return

The results showed that Free Cash Flow had no effect on Stock Return. So that H3 is rejected. In a company, investment opportunities can also affect dividend policy. Investment is one of the important indicators for companies to increase company value. Company value can be seen from the stock market value indicator which is influenced by investment opportunities. Free Cash Flow has made interests different between the "principal" and "agent" where the principal or principal wants a return on the results of his investment while the agent wants the company to hold the first profit for the expansion of his company. The higher the Free Cash Flow" (Free Cash Flow) in a company, the company has the ability to grow and develop. Because with a high free cash flow indicates high company performance. High free cash flow also illustrates the growth of cash creation in the future. High company performance will increase shareholder value which is realized in the form of higher returns through dividends, stock prices, or retained earnings to be invested in the future." (Suhartono, 2021). Risanta & Ulfah, (2022) states that funding activity cash flow and accounting profit have no significant effect on stock returns. The higher the value of cash flow owned by the company, the greater the company's stock return, because the capital gain from the stock is getting bigger. This happens because companies can use discretionary free cash flow such as acquisitions, growth-oriented capital expenditures, debt payments, and dividend payments (Tumakaka, 2021). While research Ayu et al.,)2015) states that cash flow from operating activities has no significant effect on stock returns, cash flow from funding activities has no significant effect on stock returns.

Agency Cost Impact on Operating Performance

The results showed that Agency Cost affects Operating Performance. So that H4 is accepted. These results are supported by Komarudin et al., (2019) that agency cost has an insignificant effect on company performance. The existence of a negative agency cost effect on company performance is because management will not care about operating costs so that the company's goals are not necessarily achieved by lower operating costs. By the company shows that the company is not efficient in controlling its operating costs. This will cause the profits earned by the company to decrease.

Operating cash flow is used by creditors to determine the company's ability to pay debt. If the company cannot pay the debt at maturity. Companies that have high operating cash flow, it can be interpreted that the company has good resources in carrying out its operating activities. Conversely, if the company's operating cash flow is low, then the company does not have good resources in its operating activities (Septiyaning, 2021). Hidayat, (2017) states that Agency Cost Impact has a significant negative effect on Operating Performance.

Agency Cost Impact on Firm Value

The results showed that Agency Cost affects Firm value. So that H5 is accepted. High agency costs indicate the existence of agency problems or conflicts of interest between shareholder and management. Management tends to prioritize their personal interests in acting by ignoring the interests of shareholders, such as making investment decisions in bad investment choices that can reduce the firm operational performance. A high agency cost value also reducing investor confidence in the firm which can result in negative sentiment towards the share price which is the main component in calculating firm value and stock returns (Santry Afriani Dewi et al., 1970). Supported by Nurmalasari & Yani, (2021) which concluded that there is no significant influence between agency costs as measured by two alternative efficiency ratios on firm value.

Agency Cost Impact on Stock Return

The results showed that Agency Cost has an effect on Stock Return. So that H6 is accepted. The results of this study are supported by Steven, (2019) which states that Agency Cost has a negative but insignificant effect on stock returns. Agency cost is the cost arising from the information gap between management and shareholders (principal) (Nurmalasari & Maradesa, 2021). Of course, the

agency cost to reduce the agency conflict will also be greater (Lailiyah & Abadi, 2021). The higher the agency cost, the company value will decrease (Nurmalasari & Yani, 2021). In contrast to the results of Nurkharomi et al., (2017) research which states that agency cost has no effect on stock returns.

CONCLUSION

Research results can be concluded that free cash flow has no positive significant effect on firm performance with return on asset, tobin's q ratio and holding period return as proxies. These results denied first, second and third hypothesis in this research and also doesn't empirically support free cash flow hypothesis by Jensen (1986).

Free cash flow has no significant effect on firm value, it is possible because of some reasons. Firm does not always used their free cash flow for activities that have direct effect on performance. most of the firm hold free cash flow for spare in case situation going bad for the firm. High debt also makes firm does not have enough free cash flow to invest to improve firm performance. Free cash flow is the historical performance result while firm value is the investor future expectation of the firm. Firm value and share return using share price as a main component for the calculation. Share price is determined by many factors that firm could not control. Second, agency cost has a negative significant effect on firm performance with return on asset, tobin's q ratio and holding period return as proxies. These results accept the fourth, fifth and sixth hypothesis in this research and also could give empirical evidence to support free cash flow hypothesis by Jensen (1986).

Based on agency theory, conflict of interest forces shareholder (principal) creates monitoring devices to control managers (agents) to act and make decisions with shareholder interest. The cost resulting from potential of agency problem is agency cost. Costs directly reduced profits which reduce firm performance. High agency cost is the signal of agency problem and could reduce investor confidence. That could give negative sentiment to firm share price that affect firm value and share return.

This study still has many shortcomings. Proxies of agency cost still not clearly defined in the previous study. This study only used one proxy for agency cost (operating expenses ratio) due to lack of data in Indonesia Stock Exchange. Operating expenses ratio is indirect proxy for agency cost. This study also does not include qualitative elements for agency cost measured. This study only used two control variables. For future research, it is suggested to used more proxies for agency cost and explore more control variable that related to the firm performance.

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