

# Investigating the Impact of Stock Trading Volume, Market Capitalization, and Dividend Policy on Stock Returns: Challenges and Strategic Insights

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## Abstract

*This study examines the influence of trading volume, market capitalization, and dividend policy on stock returns of LQ45 companies listed on the Indonesia Stock Exchange from 2019 to 2023. Using a quantitative approach with purposive sampling and panel data regression analysis, the study analyzes 65 observations from 13 firms based on annual reports. The results indicate that all variables jointly affect stock returns. Partially, market capitalization has a significant positive effect, trading volume is not significant, and dividend policy has a significant negative effect. These findings suggest that stock returns in Indonesia are predominantly driven by firm fundamentals rather than market activity indicators. Trading activity may reflect short-term speculative behavior rather than fundamental value. By integrating signaling theory, market efficiency theory, and asset pricing theory, this study provides a comprehensive explanation of stock return determinants.*

**Keywords:** Trading Volume, Market Capitalization, Dividend Policy, Stock Returns, LQ45 Index.

**JEL Classification:** G32, C22

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## Introduction

The stock market plays a crucial role in capital allocation by facilitating the exchange of financial instruments such as stocks and bonds. In Indonesia, the LQ45 Index represents a group of highly liquid and large-cap companies, making it a key reference for both institutional and retail investors. Understanding the determinants of stock returns in this context is essential for developing effective investment strategies and improving market efficiency.

Prior studies have extensively examined the influence of financial variables such as trading volume, firm size, and dividend policy on stock returns. However, the findings remain inconclusive, particularly in emerging markets where informational inefficiencies and behavioral biases are more pronounced. Empirical evidence suggests that trading activity is often driven by investor attention and speculative behavior rather than purely fundamental information, which may weaken its ability to predict stock returns. Consistent with this, several studies in the Indonesian context also find that trading volume does not always have a significant effect on stock returns (Wibowo & Hendratno, 2019; Nessa, 2023).

Firm size, commonly proxied by market capitalization, has long been recognized as an important determinant of stock returns. Larger firms tend to be more stable and less risky, which makes them more attractive to investors. However, the magnitude and direction of this effect may vary depending on market conditions and firm characteristics. Empirical findings in Indonesia support this argument, showing that market capitalization can positively influence stock returns, although the results are not always consistent (Agustinus et al., 2020; Gea & Anggraini, 2020).

Meanwhile, dividend policy remains a key factor in investment decision-making. From a signaling perspective, dividend payments can convey information about a firm's future prospects, although high dividend payouts may also indicate limited growth opportunities. Empirical studies further show that dividend policy has varying effects on stock returns depending on firm performance and financial conditions (Kholifah & Retnani, 2021; Ningsih & Maharani, 2022).

Overall, previous studies indicate that trading volume, market capitalization, and dividend policy do not always produce consistent or significant effects on stock returns. These inconsistencies are influenced by differences in market conditions, firm characteristics, and investor behavior, as well as external shocks such as economic crises and market volatility (Charara et al., 2023; Rahmanissa & Isyuardhana, 2022; Haryanto, 2020).

Despite the extensive body of literature examining trading volume, market capitalization, and dividend policy, several critical gaps remain insufficiently addressed. First, prior studies predominantly analyze these variables in isolation, without integrating the underlying theoretical frameworks that explain their interactions. In particular, the linkage between signaling theory, market efficiency theory, and asset pricing theory has not been explicitly synthesized in a unified empirical model. Second, empirical findings remain inconsistent across emerging markets, suggesting that the determinants of stock returns are highly context-dependent and influenced by behavioral biases, information asymmetry, and market inefficiencies. This indicates a lack of a comprehensive framework that captures both fundamental and behavioral dimensions simultaneously. Third, limited studies incorporate robustness approaches to validate the stability of regression results, particularly by controlling for macroeconomic and firm-specific factors.

Despite the extensive body of literature examining trading volume, market capitalization, and dividend policy, several critical gaps remain insufficiently addressed. First, prior studies predominantly analyze these variables in isolation, without integrating the underlying theoretical frameworks that explain their interactions. Second, empirical findings remain inconsistent, particularly in emerging markets, where stock return dynamics are influenced by both fundamental factors and behavioral biases. Third, limited studies explicitly examine whether stock returns are primarily driven by firm fundamentals or market activity indicators.

Therefore, this study aims to address these gaps by integrating Signaling Theory, Market Efficiency Theory, and Fama-French Five Factor Model into a unified empirical framework. Specifically, this study investigates whether stock returns in the Indonesian LQ45 index are predominantly influenced by firm fundamentals, represented by market capitalization and dividend policy, or by market activity indicators such as trading volume. By doing so, this study provides a more comprehensive and theoretically grounded explanation of stock return determinants in an emerging market context.

## **Literature Review**

### **Theoretical Framework Integration**

This study is grounded in three major theoretical perspectives: signaling theory, market efficiency theory, and asset pricing theory. From the perspective of **signaling theory**,

corporate financial decisions such as dividend policy convey information about a firm's future prospects. Dividend distributions may signal financial strength, but excessive payouts may also indicate limited growth opportunities. Meanwhile, **market efficiency theory** posits that stock prices reflect all available information. However, in emerging markets, informational inefficiencies and behavioral biases may weaken this mechanism, causing trading volume to reflect noise rather than fundamental value.

In addition, **asset pricing theory**, particularly the Fama-French framework, highlights firm size (market capitalization) as a systematic factor influencing expected returns. Larger firms are generally associated with lower risk and higher investor confidence. By integrating these three perspectives, this study develops a more comprehensive framework in which: (1) trading volume reflects behavioral and informational dynamics, (2) market capitalization captures fundamental firm characteristics, and (3) dividend policy represents managerial signaling decisions.

This integrated approach enables a deeper understanding of stock return formation in emerging markets.

Empirical evidence from the Indonesian Financial Review further supports the importance of financial fundamentals in explaining stock performance. Financial performance indicators have been found to significantly influence stock prices, highlighting the dominance of firm-specific fundamentals in market valuation (Agustin & Octovian, 2025). Similarly, return on equity has a significant effect on stock returns, while leverage does not, indicating that not all financial variables consistently influence market outcomes (Lubis & Nur Alfiyah, 2021).

The relationship between trading volume, market capitalization, and stock returns has been widely examined in financial literature, producing diverse and sometimes contradictory findings. Trading volume is commonly interpreted as a proxy for investor sentiment and market liquidity, both of which can influence stock price movements. Higher trading volumes are generally associated with increased investor interest and market activity, which may enhance stock performance (Wibowo & Hendratno, 2019). However, trading volume does not always reflect fundamental information, as it can also be driven by investor attention and speculative behavior, thereby weakening its predictive power for stock returns (Barber et al., 2022; Nessa, 2023).

From the perspective of **market efficiency theory**, stock prices are expected to fully reflect all available information. In an efficient market, trading volume should incorporate relevant information into stock prices, leading to predictable return patterns. However, in emerging markets, where informational asymmetry and behavioral biases are more prevalent, trading activity may reflect noise trading rather than value-relevant information, resulting in inconsistent relationships with stock returns.

Market capitalization, defined as the total market value of a company's outstanding shares, is another important determinant of stock returns. Larger firms are often perceived as more stable and less risky, leading to more consistent returns (Gea & Anggraini, 2020). This relationship is supported by **asset pricing theory**, particularly the multi-factor model, which identifies firm size as a key factor influencing expected returns (Fama & French, 2015). Nevertheless, empirical evidence suggests that the size effect is not always consistent, as smaller firms may offer higher returns due to greater risk exposure and growth potential (Maysie, 2021; Hou et al., 2021).

In addition, firm size has been widely recognized as an important determinant of firm value and stock performance. Firm size plays a crucial role in shaping firm value, reinforcing the argument that larger firms tend to exhibit stronger market credibility and stability (Sari et al., 2025). This supports the positive relationship between market capitalization and stock returns identified in this study.

Dividend policy also plays a significant role in shaping investor behavior and stock valuation. According to **signaling theory**, dividend payments convey information about a firm's financial condition and future prospects. Firms that distribute stable dividends are often perceived as financially sound, which can increase investor confidence and positively affect stock returns (Kholifah & Retnani, 2021). However, dividend payments can also be interpreted as a signal of limited reinvestment opportunities, leading to negative market reactions (Cahyati et al., 2022). This dual interpretation is further supported by the **life-cycle theory of dividends**, which suggests that mature firms are more likely to distribute dividends due to fewer growth opportunities (DeAngelo et al., 2006; Baker & Weigand, 2022).

In addition to firm-specific factors, external conditions such as macroeconomic instability and market volatility also influence stock performance. Economic disruptions, including the COVID-19 pandemic, have demonstrated how external shocks can significantly affect investor sentiment, liquidity, and return dynamics (Haryanto, 2020; Baker et al., 2021).

Furthermore, liquidity and trading activity are closely related to stock return behavior, particularly in emerging markets where market inefficiencies are more pronounced (Chordia et al., 2001; Dang et al., 2022).

Previous IFR studies also reveal inconsistencies in the significance of explanatory variables. For example, profitability significantly affects stock returns, while operational efficiency indicators may not exhibit a significant impact (Oktrima & Indriani, 2025). This suggests that stock return determinants are highly context-dependent and cannot be explained by a single factor.

Overall, the existing literature suggests that the relationships between trading volume, market capitalization, and dividend policy on stock returns are complex and context-dependent. The inconsistencies in prior findings indicate that these variables do not operate independently but are influenced by theoretical mechanisms such as market efficiency, asset pricing, and signaling effects. Therefore, this study seeks to provide a more integrated analysis by examining these variables simultaneously within the context of companies listed in the LQ45 Index.

## **Research Methods**

This study employs a quantitative research design using purposive sampling to examine the impact of trading volume, market capitalization, and dividend policy on stock returns of companies listed in the LQ45 Index. The analysis is based on secondary data obtained from annual reports, aiming to provide empirical evidence on stock return determinants in an emerging market context.

### **Research Design**

This research adopts an associative quantitative approach to analyze the relationships between independent variables, trading volume, market capitalization, and dividend policy, and the dependent variable, stock returns. This approach enables a systematic evaluation of causal relationships using panel data analysis.

### **Population and Sample**

The population consists of all companies included in the LQ45 index during the period 2019–2023. A purposive sampling technique is applied to select firms that meet the following criteria: (1) consistently listed in the LQ45 index during the observation period, (2) provide complete annual reports and financial statements, and (3) distribute dividends during the study period. Based on these criteria, 13 companies are selected, resulting in 65 firm-year observations. The use of purposive sampling is appropriate for this study as it ensures that only firms with complete and consistent financial data are included in the analysis. This approach enhances the reliability and validity of empirical results, particularly in panel data studies where data availability and consistency are critical. Furthermore, the selected sample represents firms that meet strict criteria within the LQ45 index, thereby maintaining analytical relevance while minimizing potential bias.

### Data Collection and Variable Measurement

The study utilizes secondary data sourced from publicly available annual reports. The operational definitions of variables are as follows:

- **Stock Returns (Y):** Measured as the percentage change in stock price between two consecutive periods.

$$R = \frac{P_t - P_{t-1}}{P_{t-1}}$$

- **Trading Volume (X<sub>1</sub>):** Measured as the ratio of total shares traded to total shares outstanding, reflecting market activity and liquidity.
- **Market Capitalization (X<sub>2</sub>):** Measured as the total market value of a firm's outstanding shares, representing firm size.
- **Dividend Policy (X<sub>3</sub>):** Proxied by the Dividend Payout Ratio (DPR), calculated as follows:

$$DPR = \frac{\text{Dividend per Share}}{\text{Earnings per Share}} \times 100\%$$

**Table 1 Operational Variables**

Variable	Type	Definition	Measurement	Scale
Stock Return	Dependent	The level of return obtained by investors from stock	$R = P_t - P_{t-1} / P_{t-1}$	Ratio

Variable	Type	Definition	Measurement	Scale
(R)		price changes over a specific period		
Trading Volume (TV)	Independent	The level of trading activity reflecting investor interest and market liquidity	Total shares traded / Total shares outstanding	Ratio
Market Capitalization (MC)	Independent	The total market value of a company's outstanding shares, representing firm size	Share price × Number of shares outstanding	Ratio
Dividend Policy (DPR)	Independent	The proportion of earnings distributed as dividends to shareholders	DPR = Dividend per Share / Earnings per Share x 100%	Ratio

### Data Analysis Technique

Data analysis is conducted using panel data regression with the assistance of EViews software. The analysis consists of several stages:

1. **Descriptive Statistics**, to summarize the characteristics of the data.
2. **Classical Assumption Tests**, including normality, multicollinearity, heteroskedasticity, and autocorrelation tests, to ensure model validity.
3. **Panel Regression Analysis**, to estimate the relationships between independent and dependent variables.

To enhance robustness, the appropriate panel data model (Common Effect, Fixed Effect, or Random Effect) is selected based on model specification tests such as the Chow test, Hausman test, and Lagrange Multiplier test.

### Hypothesis Testing

Hypothesis testing is conducted using the F-test to assess the joint significance of all independent variables and the t-test to evaluate the partial effects of each variable. The significance level is set at 5% ( $\alpha = 0.05$ ). The hypotheses tested in this study are as follows:

- H1: Trading Volume, Market Capitalization, and Dividend Policy simultaneously affect Stock Returns.
- H2: Trading Volume affects Stock Returns.
- H3: Market Capitalization affects Stock Returns.
- H4: Dividend Policy affects Stock Returns.

### **Panel Data Model Specifications**

To ensure robust estimation, three panel data approaches are applied:

#### **Common Effect Model (CEM)**

$$R_{it} = \alpha + \beta_1 TV_{it} + \beta_2 MC_{it} + \beta_3 DPR_{it} + \varepsilon_{it}$$

This model assumes homogeneity across cross-sectional units and time periods.

#### **Fixed Effect Model (FEM)**

$$R_{it} = \alpha_i + \beta_1 TV_{it} + \beta_2 MC_{it} + \beta_3 DPR_{it} + \varepsilon_{it}$$

This model accounts for unobserved heterogeneity across firms by allowing individual-specific intercepts.

#### **Random Effect Model (REM)**

$$R_{it} = \alpha + \beta_1 TV_{it} + \beta_2 MC_{it} + \beta_3 DPR_{it} + u_i + \varepsilon_{it}$$

This model assumes that individual-specific effects are random and uncorrelated with the independent variables.

### **Model Selection Procedure**

The selection of the most appropriate panel data model was conducted through a series of specification tests to ensure the robustness and validity of the estimation results.

First, the **Chow Test** was applied to determine whether the Common Effect Model (CEM) or the Fixed Effect Model (FEM) is more appropriate. This test evaluates the presence of individual heterogeneity across cross-sectional units. Second, the **Hausman Test** was employed to choose between the Fixed Effect Model (FEM) and the Random Effect Model

(REM). The test examines whether individual effects are correlated with the independent variables, thereby determining the consistency of the estimator. Third, the **Lagrange Multiplier (LM) Test** was used to compare the Common Effect Model (CEM) and the Random Effect Model (REM). This test identifies whether random effects are present and whether the REM provides a more efficient estimation than the CEM. Through these sequential tests, the most appropriate model was selected based on statistical significance and theoretical consistency, ensuring that the final model adequately captures both cross-sectional and time-series variations in the data.

**Table 2 Expected Signs of Coefficients**

<b>Variable</b>	<b>Expected Sign</b>	<b>Explanation</b>
Trading Volume (TV)	±	May reflect investor attention or noise trading
Market Capitalization (MC)	+	Larger firms tend to be more stable
Dividend Policy (DPR)	±	Can signal strength or limited growth

### **Interpretation of the Model**

$\beta_1$ : Measures the impact of trading activity on stock returns

$\beta_2$ : Captures the effect of firm size on stock returns

$\beta_3$ : Reflects the influence of dividend policy on stock returns

## **Results and Discussions**

### **Results**

#### **Descriptive Statistics**

**Table 3 Descriptive Statistics**

Statistics	Stock Return	Trading Volume	Market Capitalization	Dividend Policy
<b>Mean</b>	-0.035724	0.059039	2.41E+14	0.506581
<b>Median</b>	-0.026613	0.054401	1.35E+14	0.444982
<b>Maximum</b>	0.358506	0.282809	1.16E+15	0.999274
<b>Minimum</b>	-0.734548	0.000635	2.80E+13	-0.073258
<b>Std. Dev.</b>	0.204346	0.050596	2.56E+14	0.262618
<b>Observations</b>	65	65	65	65

Source: Output Eviews ver-12 (2025)

The descriptive statistics in Table 2 provide an overview of the distributional characteristics of the variables used in this study. Stock returns exhibit a negative mean value of  $-0.0357$ , indicating that, on average, firms experienced a slight decline in returns during the observation period. The median ( $-0.0266$ ) is higher than the mean, suggesting a moderately left-skewed distribution driven by extreme negative values, as reflected in the minimum return of  $-0.7345$ . The relatively high standard deviation ( $0.2043$ ) indicates substantial volatility in stock performance. Trading volume shows a mean of  $0.0590$  and a median of  $0.0544$ , implying a symmetric distribution with moderate dispersion (standard deviation =  $0.0506$ ). The relatively small gap between minimum and maximum values suggests that trading activity is comparatively stable across observations.

Market capitalization demonstrates a large mean value ( $2.41 \times 10^{14}$ ) with a median of  $1.35 \times 10^{14}$ , indicating a right-skewed distribution where a few large firms dominate the sample. This is further confirmed by the high standard deviation ( $2.56 \times 10^{14}$ ), reflecting significant heterogeneity in firm size.

Dividend policy has a mean of  $0.5066$  and a median of  $0.4450$ , suggesting that, on average, firms distribute approximately half of their earnings as dividends. The wide range, from  $-0.0733$  to  $0.9993$ , indicates variability in payout behavior, with some firms exhibiting negative or near-zero payouts. The standard deviation ( $0.2626$ ) confirms moderate variation

across firms. Overall, the descriptive statistics suggest notable variability across variables, particularly in stock returns and market capitalization, which may have important implications for subsequent regression analysis.

### Panel Data Regression Analysis

**Table 4 Common Effect Model**

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<b>Variable</b>	<b>Coefficient</b>	<b>Std. Error</b>	<b>t-Statistic</b>	<b>Prob.</b>
<b>C</b>	0.019248	0.061848	0.311224	0.7567
<b>X1_TVA</b>	0.357953	0.494586	0.723743	0.4720
<b>X2_KP</b>	2.02E-16	9.53E-17	2.121154	0.0380
<b>X3_DPR</b>	-0.246358	0.093884	-2.624052	0.0110

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Source: Output Eviews ver-12 (2025)

**Table 5 Fixed Effect Model**

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<b>Variable</b>	<b>Coefficient</b>	<b>Std. Error</b>	<b>t-Statistic</b>	<b>Prob.</b>
<b>C</b>	0.104488	0.090320	1.156859	0.2529
<b>X1_TVA</b>	-0.395269	0.862823	-0.458111	0.6489
<b>X2_KP</b>	-3.78E-17	1.88E-16	-0.200890	0.8416
<b>X3_DPR</b>	-0.212733	0.110457	-1.925940	0.0599

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Source: Output Eviews ver-12 (2025)

**Table 6 Random Effect Model**

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<b>Variable</b>	<b>Coefficient</b>	<b>Std. Error</b>	<b>t-Statistic</b>	<b>Prob.</b>
<b>C</b>	0.019248	0.063973	0.300886	0.7645
<b>X1_TVA</b>	0.357953	0.511578	0.699703	0.4868

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<b>Variable</b>	<b>Coefficient</b>	<b>Std. Error</b>	<b>t-Statistic</b>	<b>Prob.</b>
<b>X2_KP</b>	2.02E-16	9.86E-17	2.050699	0.0446
<b>X3_DPR</b>	-0.246358	0.097110	-2.536892	0.0138

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Source: Output Eviews ver-12 (2025)

**Table 7 Chow Test**

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<b>Effects Test</b>	<b>Statistic</b>	<b>d.f.</b>	<b>Prob.</b>
Cross-section F	0.667916 (12, 49)		0.7729
Cross-section Chi-square	9.847101	12	0.6294

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Source: Output Eviews ver-12 (2025)

**Table 8 Lagrange Multipilier**

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<b>Test</b>	<b>Statistic</b>	<b>Prob.</b>
Cross-section	2.042183	0.1530
Time	5.865162	0.0154
Both (Cross-section & Time)	7.907345	0.0000

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Source: Output Eviews ver-12 (2025)

**Table 9 Panel Data Model Selection**

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<b>No.</b>	<b>Test</b>	<b>Model Comparison</b>	<b>Selected Model</b>
1	Chow Test	Common Effect vs. Fixed Effect	Common Effect
2	Hausman Test	Fixed Effect vs. Random Effect	Not Performed
3	Lagrange Multiplier Test	Common Effect vs. Random Effect	Common Effect

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Source: Output Eviews ver-12 (2025)

## Regression Results and Hypothesis Testing

The panel data regression analysis using the Common Effect Model (CEM) was conducted to examine the influence of trading volume, market capitalization, and dividend policy on stock returns.

### **F-Test Results**

The F-statistics are 3.836 with a probability value of 0.0139, which is below the 0.05 significance level. This indicates that all independent variables jointly have a statistically significant effect on stock returns. Therefore, H1 is accepted, confirming that trading volume, market capitalization, and dividend policy simultaneously influence stock returns.

### **t-Test Results**

#### **Trading Volume (X1)**

Trading volume has a t-statistic of 0.724 and a p-value of 0.472 ( $> 0.05$ ), indicating no statistically significant effect on stock returns. Thus, H2 is rejected. This finding suggests that trading activity does not necessarily reflect firm fundamentals or investor valuation in this sample and may instead be driven by short-term speculative behavior.

#### **Market Capitalization (X2)**

Market capitalization shows a t-statistic of 2.121 with a p-value of 0.038 ( $< 0.05$ ), indicating a significant positive effect on stock returns. Therefore, H3 is accepted. This result supports the argument that larger firms tend to exhibit greater stability, lower perceived risk, and stronger investor confidence, which contributes to higher stock returns.

#### **Dividend Policy (X3)**

The findings of this study provide a more integrated and theoretically grounded explanation of stock return determinants within the context of emerging markets. The significant positive effect of market capitalization on stock returns confirms the critical role of firm size as a key determinant of investor preference. From an asset pricing perspective, larger firms are generally associated with lower risk, greater financial stability, and stronger market credibility, which enhance investor confidence and lead to higher expected returns. This result reinforces the firm size effect and highlights its continued relevance in the Indonesian capital market (Gea & Anggraini, 2020; Rahmanissa & Isynuwardhana, 2022).

In contrast, trading volume does not exhibit a statistically significant effect on stock returns, suggesting that trading activity alone is not a reliable proxy for firm value. This finding indicates that market behavior may be dominated by noise trading and investor sentiment, rather than value-relevant information. Within the framework of market efficiency theory, this result implies that the Indonesian stock market may not fully incorporate trading signals into price formation. Instead, trading volume appears to reflect short-term speculative behavior, thereby weakening its explanatory power for stock returns (Nessa, 2023; Maysie, 2021; Susanto & Kartawinata, 2023).

Furthermore, dividend policy is found to have a significant negative effect on stock returns, providing important insights into how investors interpret dividend signals. Although dividend payments are traditionally associated with positive signaling, excessively high dividend payouts may indicate limited reinvestment opportunities and reduced future growth prospects. From the perspective of signaling theory and residual dividend theory, firms that prioritize dividend distribution over investment may be perceived as having reached a mature stage with constrained expansion potential. Consequently, such signals may lead to less favorable investor responses and lower stock returns (Cahyati et al., 2022; Ningsih & Maharani, 2022).

## **Discussion**

The findings of this study directly address the research gap identified in the introduction regarding the relative importance of firm fundamentals and market activity indicators in explaining stock returns. The results clearly indicate that stock returns in the Indonesian LQ45 index are predominantly driven by firm fundamentals rather than trading activity, confirming that in emerging markets, fundamental factors play a more critical role than short-term market signals in shaping stock performance.

Specifically, the significant positive effect of market capitalization confirms that firm size plays a dominant role in influencing stock performance. Larger firms tend to exhibit stronger financial stability, lower risk exposure, and higher investor confidence, which ultimately leads to more consistent returns. This finding is consistent with asset pricing theory, particularly the Fama-French Five Factor Model, which identifies firm size as a key systematic factor in determining expected returns. Empirical evidence from Indonesian Financial Review studies also supports this argument, emphasizing the importance of firm fundamentals in shaping stock valuation (Agustin & Octovian, 2025; Sari et al., 2025). This

result is further reinforced by prior empirical findings that highlight the positive influence of market capitalization on stock returns (Gea & Anggraini, 2020; Rahmanissa & Isyнуwardhana, 2022).

In contrast, trading volume does not exhibit a significant effect on stock returns, suggesting that trading activity may not reflect fundamental firm value. This result indicates the presence of noise trading and speculative behavior in the market, where investors base their decisions on short-term signals rather than underlying company performance. From the perspective of Market Efficiency Theory, this finding implies that the Indonesian stock market may not fully incorporate trading information into price formation, reflecting a degree of market inefficiency. Similar findings have been documented in IFR studies, where activity-based variables often fail to demonstrate consistent explanatory power (Oktrima & Indriani, 2025). In addition, prior studies also report that trading volume does not consistently affect stock returns and may be driven by investor attention and speculative behavior (Wibowo & Hendratno, 2019; Nessa, 2023; Susanto & Kartawinata, 2023).

Furthermore, dividend policy is found to have a significant negative effect on stock returns, providing strong evidence of how investors interpret dividend signals. While dividends are traditionally associated with positive signaling, excessively high dividend payouts may indicate limited reinvestment opportunities and reduced future growth potential. This interpretation is consistent with Signaling Theory and the life-cycle theory of dividends, which suggest that mature firms tend to distribute higher dividends due to fewer growth opportunities. Empirical support from IFR studies also confirms that dividend policy may generate adverse market reactions when interpreted as a signal of declining growth prospects (Lubis & Nur Alfiyah, 2021). This finding is further supported by previous studies indicating that dividend policy may negatively influence stock returns under certain conditions (Cahyati et al., 2022; Ningsih & Maharani, 2022).

Overall, these findings highlight that stock return determinants in emerging markets are primarily driven by firm fundamentals rather than market activity indicators. The results also emphasize the importance of integrating multiple theoretical perspectives to better understand stock market behavior in environments characterized by informational inefficiencies and behavioral biases. These results are also consistent with prior literature emphasizing the role of liquidity, market conditions, and external shocks in shaping stock return dynamics (Chordia et al., 2001; Dang et al., 2022; Haryanto, 2020).

Overall, this study demonstrates that stock return dynamics are primarily driven by firm fundamentals rather than market activity indicators. By integrating signaling theory, market efficiency theory, and asset pricing theory, this research offers a more comprehensive framework for understanding how trading behavior, firm size, and financial policy interact in shaping stock performance. These findings underscore the importance of fundamental analysis for investors and highlight the need for firms to adopt balanced financial strategies that support sustainable growth and long-term value creation.

## **Conclusions**

This study examines the effect of trading volume, market capitalization, and dividend policy on stock returns of companies included in the LQ45 index on the Indonesia Stock Exchange during the 2019–2023 period. The findings provide a clear answer to the research gap identified in the introduction regarding the relative importance of firm fundamentals and market activity indicators in explaining stock returns.

The empirical results demonstrate that stock returns in the Indonesian capital market are predominantly driven by firm fundamentals rather than market activity. Market capitalization is found to have a significant positive effect on stock returns, confirming that firm size plays a crucial role in shaping investor confidence and market performance. In contrast, trading volume does not exhibit a significant effect, indicating that trading activity may reflect short-term speculative behavior rather than fundamental value. Furthermore, dividend policy has a significant negative effect on stock returns, suggesting that higher dividend payouts may be interpreted by investors as a signal of limited growth opportunities.

These findings reinforce the importance of integrating Signaling Theory, Market Efficiency Theory, and Fama-French Five Factor Model in explaining stock return dynamics, particularly in emerging markets characterized by informational inefficiencies and behavioral biases. The results also contribute to the literature by providing empirical evidence that challenges the assumption that market activity indicators play a dominant role in determining stock returns.

From a practical perspective, these findings suggest that investors should prioritize fundamental analysis, particularly firm size and financial policy, rather than relying solely on

trading signals. For corporate managers, the results highlight the importance of balancing dividend distribution with reinvestment strategies to support long-term growth and firm value.

For future research, it is recommended to incorporate additional variables such as macroeconomic indicators (e.g., inflation, interest rates, and economic growth) and behavioral factors such as investor sentiment to better capture the complexity of stock return dynamics. Expanding the sample across sectors and extending the observation period may also enhance the generalizability of the findings. Overall, this study provides a more comprehensive and theoretically grounded understanding of stock return determinants in the Indonesian capital market.

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