Institutional Ownership, Types of Industry, and Income Smoothing: Empirical Evidence from Indonesia

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Abstract; This paper aims to evaluate the impact of institutional ownership and types of industry on income smoothing in the Indonesian listed firms. Base on literatures and employing panel data approach, it examines 112 firms listed on the Indonesia Stock Exchange during 2012 to 2016 periods (i.e., 560 observations). By using OLS regression to test the hypotheses, the findings indicate the institutional ownership does not affect significantly on income smoothing practice. Moreover, types of industry do not influence on income smoothing practices, except for consumer goods industry which affect significantly on income smoothing practice. Considering the company size as a control variable, the result shows that company size influences positively on income smoothing practice. Therefore, this study contributes in providing empirical evidence on the relationship between institutional ownership, types of industry, and income smoothing practice in emerging market context (i.e., Indonesia).

INTRODUCTION

Financial statements are commonly used as one of the indicators to evaluate information related to a company; and hence it tends to encourage managers to manipulate the data presented in the financial statements to get a good impression from the users of the financial statements. Even tough, managers must present financial statements that are not fit with their actual performance, which can be done by income smoothing practice that is expected to create a better presented information with regard to the company financial information (i.e, financial position, performance, and so-forth). Income smoothing is defined as the spread of intentional rate fluctuations that are currently considered normal for a company (Biedleman, 1973). While Koch (1981) defines income smoothing as a means used by managers to reduce the variability in reported revenue streams.

The income smoothing practice is a common phenomenon in a company when an asymmetric information occurred between managers and shareholders because of the separation of ownership and control. This condition causes managers to have more information about the company than shareholders and often managers take an advantage from information they have in order to pursue their personal interests (Jensen & Meckling, 1976). As an agent, managers tend to improve presentation of the financial statements that can be done by income smoothing; so that it looks like to have a good performance in front of the shareholders. In other words, managers will exhibit their opportunistic behavior through income smoothing activities.

Li and Richie (2016) explained that there are two managers’ motivations in conducting the income smoothing, i.e., signaling and garbling. Earnings’ information as a signal to investors is more informative than earnings’ information as a garbling. Koch (1981) argued that income smoothing is a managerial’s tool to reduce variability of reported earnings for certain purpose by manipulating artificial variables (accounting) or real variables (transaction). Moreover, Eckel (1981) explained two types of income smoothing, i.e, naturally smooth and intentionally smooth, which the intentionally smooth consists of artificial smoothing and real smoothing. Previous studies have documented that one of the motivations that drives managers to do the income smoothing is because they want to maintain the company profitability in subsequent periods (Hunt et al., 2000; Tucker & Zarowin, 2006). In other words, income smoothing can be used by managers to increase value of corporate earnings information that is presented in the financial statements so that the users of financial statements will see that the company performance is in a good condition.

Furthermore, this study intends to evaluate two factors that may affect the opportunistic behavior of managers through the income smoothing, i.e. institutional ownership and types of industry. The present of institutional ownership of the company's stock is expected to provide a better oversight function for the company towards the behavior of managers because institutional investors usually come from large corporations that generally have more professional monitoring instruments. When the oversight function undertaken by an institution that has a shareholding in a company can run optimally then this condition will be able to prevent managers from behaving opportunistically through income smoothing practices. Furthermore, some institutions that buy corporate shares for short-term purposes also encourage the owners of these institutions to focus on achieving short-term profits, so that their supervision will be optimal to achieve this goal. On the basis of this argument, several previous studies have proved that in general institutional ownership is more capable in supervising manager behavior optimally, therefore the existence of blocks of institutional ownership in the company can be used as a mean to reduce the income smoothing practice (Bartov et al., 2000; Jiambalvo et al., 2002).

However, previous studies examining relationship between institutional ownership and income smoothing showed different results. Several previous studies from overseas countries found a negative relationship between institutional ownership and income smoothing (e.g., Bushee, 1998; Chung et al., 2002; Edmans, 2009; Hadani et al., 2011; Kalelkar & Nwaeze, 2011; and Chen et al., 2016). Meanwhile, Makaryanawati and Milani (2008) in Indonesia found that institutional ownership has no significant effect on income smoothing. In another case in Indonesia, Mahastanti and Pratiwi (2014) found that income smoothing phenomenon in Indonesian listed firms tends to be
garbling rather than signaling. In other words, it is indicating that previous research findings are depending on the country context in which the research is conducted. In developed countries such as USA and UK the average finding of previous studies indicates that the existence of institutional ownership can be a deterrent to the income smoothing practices undertaken by managers. However, the findings are totally different when the research is undertaken in developing countries such as Indonesia where the present of institutional ownership does not affect significantly on income smoothing practice. The finding indicates that the supervisory role by institutional investors is not as optimal as in developed countries. On the basis of such argumentation, this study intends to re-examine the effect of institutional ownership on income smoothing in Indonesia, with the expectation that there will be a different research finding compared to those previous studies in Indonesian which had been conducted about a decade ago such as in Makaryanawati and Milani (2008).

Types of industry is also one of factors influencing the income smoothing practices where it was confirmed by several previous studies particularly in the overseas countries. Atik (2009) found empirical evidence in Turkey showing that firms in different industries respond differently to the dynamics of economic change, and ultimately affect the level of income smoothing practice in each company. Belkaoui and Picur (1984) found that due to different conditions between major industry type and other types of industry in a capital market in the face of environmental opportunities and uncertainty, it will affect the level of income smoothing practices they do. In general, the main industry has greater competitiveness than other class of industries. Similar findings are also obtained by Mahmud (2012) who found empirical evidence in Malaysia that the types of industry affect the income smoothing practice in each company. However, some previous studies have also found that types of industry have no significant effect on the opportunistic behavior of managers in income smoothing activities (Albrecht and Richardson, 1990; Trisanti, 2014).

Based on the above explanation, the purpose of this study is to examine the effect of institutional ownership and types of industry on the income smoothing practice in companies listed on the Indonesia Stock Exchange for the 2012-2016 periods. To get an optimal picture of the relationship among variables in this study, it uses firm size as a control variable.

**LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT**

**Literature Review**

The agency theory framework is developed by Jensen and Meckling (1976) and extended by Tucker and Zarowin (2006) suggested that managers have an incentive to present variations in revenue streams to increase compensation or to reduce long-term capital costs. Healy and Wahlen (1999) explained that income smoothing is defined as the managers’ choice to report the company results of operation in order to reduce the variability of accounting income. It is accomplished by deferring earnings during the profitable years for use during the downturn years on the next periods. Furthermore, Michelson et al. (1995) explained that the income smoothing practice is an action done by management by distributing income reporting in the years with high-profit level to the following years whose profits are relatively low. As a result, the achievement of the company’s profit is always stable in each reporting period and ultimately it is intended to increase the company market returns. In other words, through the practice of income smoothing, managers hope to attract investors when investors see the company’s earnings are always stable over years. It is because investors usually put more emphasis on procedures in achieving the profits generated by companies in which they invest.

Income smoothing is the most favored way by managers to reduce the fluctuations in company earnings that are announced which shows managers effort to reduce the variation in abnormal returns within the limits permitted by accounting practices and reasonable management principles. Similarly, Belkaoui and Picur (1984) defined income smoothing as a smoothing that involves selecting repetitive accounting or reporting measurements in a particular pattern which affects on reported income streams with
variations that are smaller than the real trend that would appear when there are no smoothing activities.

Based on agency theory, the concept of income smoothing states that the practice of income smoothing is influenced by the conflict of interest between managers (agent) and the owner (principal) when each party seeks to achieve or maintain the desired level of prosperity for their interest (Jensen & Meckling, 1976). The information gap between the two parties triggers the emergence of income smoothing practice. According to Eckel (1981) the practice of income smoothing has two types, i.e., income smoothing done intentionally by management and income smoothing that occur naturally. Income smoothing naturally occurs as a result of the process of generating a uniformly distributed income stream, while intentional income smoothing occurs as a result of a real profit smoothing technique or an artificial smoothing technique. Real income smoothing is the smoothing of profits that occurs when managers take action to compile economic events resulting in a flat income stream. Income artificial smoothing is the smoothing of profits that occurs when managers manipulate the financial data during accounting records to produce stable profit stream. Therefore, it can also be concluded that the internal parties (the managers) practice income smoothing in order to meet the expectations of outside parties (i.e., the users of financial statements) so that financial statements as a description of the manager’s performance will be in a good impressed. If these conditions can be achieved then the managers will be judged as in a good performance by the shareholders as principal.

Hypotheses Development
Institutional Ownership and Income Smoothing

Institutional ownership is expected to have an optimal role in carrying out oversight function of the activities of managers, including to monitor possible opportunistic behavior of managers through the practice of income smoothing. Putri and Natsir (2006) and Hadani, et al. (2011) explained that ownership by institutional investors such as insurance companies, banks, investment companies and other institutional ownership will encourage more optimal supervision of management performance since share ownership represents a source of power that can be used to support the existence of managers. Institutional investors are often regarded as sophisticated investors who cannot easily be fooled by the actions of managers and should be better able to use current period information in predicting future earnings compared to non-institutional investors (Edmans, 2009). With these advantages, institutional investors will be able to produce a range of monitoring capabilities that can be used to limit opportunistic behavior of managers who tend to pursue their self-interest, among others, through the practice of income smoothing (Bushee, 1998; Hadani et al., 2011). In other words, the presence of institutional investors will have a better understanding of managers’ activities to prevent the occurrence of managers’ opportunistic behaviors, such as in income smoothing activities.

Through the institutional ownership, effectiveness of enterprise resource management by managers can be known from information generated through market reactions to earnings announcements. Chen et al. (2016) stated that one component of good corporate governance that also affects the practice of income smoothing is the shares owned by institution or block holder. Institutional investors are often referred to as sophisticated investors, so it is assumed to have more capability in using current information to predict future corporate profitability compared to non-institutional investors. It is because the ownership by the institutional investors has the ability to control (controlling ownership) because of the proportion of share owned by institution is normally high so that it can reduce the income smoothing practices by managers.

Several previous studies have proved that firms with a large proportion of institutional ownership tend to practice less income smoothing than those with a smaller proportion of institutional ownership (Bushee, 1998; Chung et al., 2002; Edmans 2009; Hadani et al., 2011). Furthermore, Li and Richie (2016) found that when institutional ownership levels are high, optimal monitoring by institutional investors causes managers to feel reluctant to practice income smoothing. Kalelkar and Nwaeze (2011) found relatively high earnings smoothing practices in companies with a proportion of institutional ownership below 15%, while companies with institutional
ownership above 15% are able to deter the income smoothing practices by managers. Further, Chen et al., 2016 have proven a negative relationship between institutional ownership and income smoothing. In other words, the higher the proportion of institutional ownership the more optimal the supervisory function they play. Ultimately this condition will be able to prevent opportunistic behavior of managers, as in the case of income smoothing. Based on the above arguments, the first hypothesis in this study is formulated as follows:

H1: The higher the proportion of institutional ownership in a company will further decrease the practice of income smoothing by managers

Types of Industry and Income Smoothing
Several previous studies found that conditions of a business environment will affect different types of industry differently which will impact on different responses from those industries. Therefore, managers from different types of industry will have different opportunistic behaviors in the same industry environment. Stein (1989) considers the same business environment to create different opportunities in different industries where it is found in particular conditions that managers from certain type of industry will be better able to maximize revenue than other industries. This is also evident from how an environmental condition is responded by different rates of stock price changes from each type of industry that participates in the capital market.

The above argument is supported by several previous studies which have proven that the type of industry affects income smoothing practices such as in Belkaoui and Picur (1984) in USA, Atik (2009) in Turkey, and Mahmud (2012) in Malaysia. Based on those arguments and the findings of several previous studies, the second hypothesis in this study is:

H2: types of industry affect income smoothing practice.

RESEARCH METHODOLOGY

Variables Measurement
Income Smoothing (SMOOTH)
This study measures the income smoothing activities by using a formula developed by Eckel (1981) that so-called by Eckel Index as follows:

\[
Eckel\ Index = \frac{CV\ \Delta GP}{CV\ \Delta I}
\]

\[
CV\ \Delta GP\ or\ CV\ \Delta I = \frac{\sum (\Delta X_i - \Delta X)^2}{n - 1} : \Delta X
\]

Where:
- GP = Change in profit in one period
- I = Change of income in one period
- CV = Coefficient of variation in the firm variable that is standard deviation divided by the expected value
- Xi = Change in profit (GP) or income (I) on the period of i
- X = Average change of profit (GP) or income (I)
- n = Number of years of observation

Institutional Ownership (INST)
Institutional ownership is measured by using the formula as follows (Suyono, 2016):

\[
\text{Institutional Ownership} = \frac{\text{number of shares owned by institution}}{\text{Total Outstanding Shares}} \times 100\%
\]

Types of Industry
The Indonesia Stock Exchange categorizes listed companies into 3 sectors, namely the main sectors, manufacturing sector, and service sectors. Moreover, these sectors are further detailed into 8 types of industry (IDX, 2016), i.e., (1) Various Industries (VARIND); (2) Consumer Goods Industry (CONSGOOD); (3) Basic Industry and Chemistry (BACHE), (4) Infrastructure, Utilities and Transportation (INFRAS); (5) Trade and Investment (TRADIN), (6) Mining (MINE); (7) Agriculture (AGRI); and (8) Property and Real Estate (PROPERTY). Therefore, following the categorization from The Indonesian Stock Exchange, this study measure types of industry by using 8 dummy variables based on those 8 types of industry accordingly. Score 1 is given when the company is in its type of industry and score 0 is given if otherwise. However, because there are 8 dummy variables, thus 1 dummy variable will be automatically excluded from the regression (Gujarati & Porter, 2009).

**Company Size (Size)**

Company size as a control variable is measured by the natural logarithm of total assets (Suyono, 2016).

**The Sample of The Study**

Implementing purposive sampling in sampling selection processes, this study ended up with 112 companies for 5 year periods, i.e, 2012-2016. Therefore, there are 560 observations. Table 1 below explains the criteria for sampling selection:

<table>
<thead>
<tr>
<th>No.</th>
<th>Criteria</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Number of listed companies in The Indonesian Stock Exchange during 2012-2016 periods</td>
<td>535</td>
</tr>
<tr>
<td>2.</td>
<td>Delisted companies in The Indonesian Stock Exchange during 2012-2016 periods</td>
<td>40</td>
</tr>
<tr>
<td>3.</td>
<td>Removing financial service companies (i.e., Insurance, Banks, Financial Institutions, Securities Companies and Other Financial Sectors)</td>
<td>91</td>
</tr>
<tr>
<td>4.</td>
<td>Listed companies with an incomplete annual report</td>
<td>292</td>
</tr>
<tr>
<td></td>
<td>Total sample</td>
<td>112</td>
</tr>
<tr>
<td></td>
<td>Total observation for 5 years (2012-2016)</td>
<td>560</td>
</tr>
</tbody>
</table>

Moreover, Table 2 below presents the category of sample based on 8 types of industry.

<table>
<thead>
<tr>
<th>NO.</th>
<th>Type</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Various Industries (VARIND)</td>
<td>13</td>
</tr>
<tr>
<td>2</td>
<td>Consumer Goods Industry (CONSGOOD)</td>
<td>6</td>
</tr>
<tr>
<td>3</td>
<td>Basic Industry and Chemistry (BACHE),</td>
<td>7</td>
</tr>
<tr>
<td>4</td>
<td>Infrastructure, Utilities and Transportation (INFRAS)</td>
<td>30</td>
</tr>
<tr>
<td>5</td>
<td>Trade and Investment (TRADIN)</td>
<td>19</td>
</tr>
<tr>
<td>6</td>
<td>Mining (MINE)</td>
<td>15</td>
</tr>
<tr>
<td>7</td>
<td>Agriculture (AGRI)</td>
<td>1</td>
</tr>
<tr>
<td>8</td>
<td>Property and Real Estate (PROPERTY)</td>
<td>21</td>
</tr>
<tr>
<td></td>
<td>Total</td>
<td>112</td>
</tr>
</tbody>
</table>

**Data Analysis**

The data analysis consists of statistic descriptive, classical assumption test of multiple regression (normality, autocorrelation, multicollinearity, and heteroscedasticity) and OLS. After all of the assumptions are met, then this study performs multiple regression analysis by using OLS. The model of regression equation in this study is as follows:
SMOOTH = α + β1INST + β2VARIND + β3CONSGOOD + β4BACHE + β5INFRAS + β6TRADIN + β7MINE + β8AGRI + β9PROPERTY + β10SIZE + ε

FINDINGS AND DISCUSSION

Descriptive Statistics
Table 3 presents the descriptive statistics of variables used in this study. It shows relatively high-income smoothing practice for companies listed on the Indonesian Stock Exchange with average value is 25.60%. Moreover, it also shows a high proportion of institutional investor in the Indonesian Stock Exchange with the average value is 51.64%. Meanwhile, for the types of industry, Infrastructure, Utilities and Transportation (INFRAS) is the most with an average value of 25.89% and agriculture is the least with an average value of 0.8%.

Table 3. Descriptive Statistics

<table>
<thead>
<tr>
<th>Variable</th>
<th>N</th>
<th>Minimum</th>
<th>Maximum</th>
<th>Mean</th>
<th>Std. Deviation</th>
</tr>
</thead>
<tbody>
<tr>
<td>SMOOTH</td>
<td>560</td>
<td>-23.0170</td>
<td>0.000</td>
<td>-.256081</td>
<td>1.1401779</td>
</tr>
<tr>
<td>INST</td>
<td>560</td>
<td>.0170</td>
<td>.9870</td>
<td>.516371</td>
<td>.3131193</td>
</tr>
<tr>
<td>SIZE</td>
<td>560</td>
<td>21.8100</td>
<td>33.6000</td>
<td>28.160536</td>
<td>1.9023600</td>
</tr>
<tr>
<td>VARIND</td>
<td>560</td>
<td>0.0000</td>
<td>1.0000</td>
<td>.080357</td>
<td>.2720884</td>
</tr>
<tr>
<td>CONSGOOD</td>
<td>560</td>
<td>0.0000</td>
<td>1.0000</td>
<td>.071429</td>
<td>.2577696</td>
</tr>
<tr>
<td>BACHE</td>
<td>560</td>
<td>0.0000</td>
<td>1.0000</td>
<td>.062500</td>
<td>.2422779</td>
</tr>
<tr>
<td>INFRAS</td>
<td>560</td>
<td>0.0000</td>
<td>1.0000</td>
<td>.258929</td>
<td>.4384379</td>
</tr>
<tr>
<td>TRADIN</td>
<td>560</td>
<td>0.0000</td>
<td>1.0000</td>
<td>.151786</td>
<td>.3591339</td>
</tr>
<tr>
<td>MINE</td>
<td>560</td>
<td>0.0000</td>
<td>1.0000</td>
<td>.160714</td>
<td>.3675956</td>
</tr>
<tr>
<td>AGRI</td>
<td>560</td>
<td>0.0000</td>
<td>1.0000</td>
<td>.008929</td>
<td>.0941524</td>
</tr>
<tr>
<td>PROPERTY</td>
<td>560</td>
<td>0.0000</td>
<td>1.0000</td>
<td>.205357</td>
<td>.4043235</td>
</tr>
<tr>
<td>Valid N</td>
<td>560</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(listwise)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Classical Assumption of Regression
Based on the classical assumption test which includes normality test, autocorrelation test, heteroscedasticity test, and multicollinearity test, the model in this study met all the criteria of classical assumption test. After all the classical assumption of regression is fulfilled then this study runs the multiple linear regression test.

Output of Regression
Table 4 above documents that from the result of regression, institutional ownership (INST) does not influence significantly on the income smoothing practices for companies listed on The Indonesian Stock Exchange. Meanwhile, types of industry generally do not influence significantly on income smoothing practices, except for consumer goods industry (CONSGOOD) which affects negatively on the income smoothing practices. Moreover, company size (SIZE) as a control variable has a positive influence on income smoothing. Then, the regression equation of this study is presented as follows:
Table 4. Output of regression Coefficients*

<table>
<thead>
<tr>
<th>Model</th>
<th>Unstandardized Coefficients</th>
<th>Standardized Coefficients</th>
<th>t</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>B</td>
<td>Std. Error</td>
<td>Beta</td>
<td></td>
</tr>
<tr>
<td>1</td>
<td>(Constant)</td>
<td>-3.981</td>
<td>1.411</td>
<td>-2.326</td>
</tr>
<tr>
<td></td>
<td>INST</td>
<td>.276</td>
<td>.265</td>
<td>.044</td>
</tr>
<tr>
<td></td>
<td>SIZE</td>
<td>.143</td>
<td>.044</td>
<td>.143</td>
</tr>
<tr>
<td></td>
<td>VARIND</td>
<td>.355</td>
<td>.347</td>
<td>.047</td>
</tr>
<tr>
<td></td>
<td>CONSGOOD</td>
<td>-1.020</td>
<td>.366</td>
<td>-.128</td>
</tr>
<tr>
<td></td>
<td>BACHE</td>
<td>-.616</td>
<td>.365</td>
<td>-.077</td>
</tr>
<tr>
<td></td>
<td>TRADIN</td>
<td>.152</td>
<td>.266</td>
<td>.028</td>
</tr>
<tr>
<td></td>
<td>MINE</td>
<td>.187</td>
<td>.267</td>
<td>.035</td>
</tr>
<tr>
<td></td>
<td>AGRI</td>
<td>-0.213</td>
<td>.890</td>
<td>-.010</td>
</tr>
<tr>
<td></td>
<td>PROPERTY</td>
<td>.137</td>
<td>.245</td>
<td>.028</td>
</tr>
</tbody>
</table>

*a. Dependent Variable: SMOOTH
F = 3.225   Sig.  0.003
R² = 0.071  Adj. R² = 0.039
INFRAS is excluded from the regression

Then, the regression equation of this study is presented as follows:

SMOOTH = -3.981 + 0.276IO + 0.355VARIND - 1,020CONSGOOD - 616BACHE + 0.152TRADIN + 0.187MINE - 213AGRI + 0.137PROPERTY + 143SIZE + ε

Discussion

The first hypothesis on this study states that the higher the proportion of institutional ownership in a company will decrease the practice of income smoothing by managers. The result of the regression analysis shows that institutional ownership of companies listed on the Indonesian stock exchange has no significant effect on the practice of income smoothing, so the first hypothesis is rejected. The findings in this study are still not able to confirm the concept of agency theory developed by Jensen and Meckling (1976) and also as explained by Tucker and Zarowin (2006) stating that the presence of institutional investors who are sophisticated investors will play an optimal role in carrying out supervisory functions on the managers’ activities. Therefore, the optimal role of supervision will create a conducive working environment; so that managers will feel reluctant to behave opportunistically such as in income smoothing activities. In other words, the existence of relatively high institutional ownership in the Indonesia Stock Exchange with an average of 51.64% is still not able to decrease the practice of income smoothing by managers where the level of income smoothing is still relatively high, i.e., 25.61%.

In other words, the findings in this study are not in line with previous studies in developed countries that were able to prove that institutional ownership is capable of lowering the practice of income smoothing (Bushee 1998; Chung et al., 2002; Edmans 2009; Hadani et al., 2011; Kalelkar and Nwaeze, 2011; and Chen et al., 2016). The results in this study are still similar to the research conducted in Indonesia a decade ago such as in Makaryanawati and Milani (2008) who found that institutional ownership does not affect the practice of income smoothing in companies listed on the Indonesia Stock Exchange.

Thus, this study proves that the concept of institutional investor supervision in developed countries like the USA which can suppress the practice of income smoothing has not been valid for Indonesian case. This indicates that the supervisory role of institutional investors has not been optimal in Indonesia, so the presence of stock ownership from a high level of institutional investors (51.64%) has no role in preventing managers from behaving opportunistically as in the income smoothing activities.
Furthermore, the second hypothesis in this study states that the types of industry affect the income smoothing practice. Regression output results show that from 8 types of industry in Indonesia Stock Exchange, only consumer goods industry (CONSGOOD) which has a significant effect on the income smoothing practice, meanwhile, the other types of industry do not have a significant influence on the income smoothing practice. Thus the second hypothesis is generally unconfirmed except for the type of consumer goods industry. In other words, the second hypothesis is partly supported only for the consumer goods industry.

This study generally proves the view that a business environment will affect different types of industries differently and impacts on the different level of income smoothing practices are less favorable, except for the type of consumer goods industry. In other words, generally the findings in this study do not match with previous research findings which have proven that the types of industry affect income smoothing practices such as in Belkaoui and Picur (1984) in USA, Atik (2009) in Turkey and Mahmud (2012) in Malaysia. However, the finding in this study generally is also in line with previous research in Indonesia (Trisanti, 2014) which states that the type of industry did not significantly affect the practice of income smoothing in companies listed on the Indonesia Stock Exchange.

With regard to the company size (SIZE) as a control variable, this study proves that firm size has a positive effect on the practice of income smoothing in companies listed on the Indonesia Stock Exchange. It means that the larger the size of the company then the possibility of income smoothing is also greater. This finding is consistent with the results of Ergin (2010) that documented that company size positively influence on income smoothing. Moreover, this finding is not in-line with Sherlita and Kurniawan (2013) Who found that company size does not affect the income smoothing practices.

**CONCLUSION AND SUGGESTIONS**

This study intends to analyze the effect of institutional ownership and types of industry on the income smoothing practice for companies listed on the Indonesia Stock Exchange for the 2012-2016 periods. By using 560 observations, it is concluded that institutional ownership has no significant effect on the income smoothing practice. Furthermore, related to the variable of types of industry, in general, this research concludes that types of industry do not have a significant effect on the income smoothing practice except for consumer goods industry which has a significant effect on the income smoothing practice.

The practical implication of the findings in this study is that the existence of institutional ownership in listed companies in the Indonesia Stock Exchange has not been able to carry out an optimal supervisory role so that the presence of this type of investor is not strong enough to prevent managers from income smoothing activities that are opportunistic behavior detrimental to the company. It is therefore advisable for these companies to be able to evaluate the role of institutional ownership so that ultimately the existence of these investors can play an optimal role in conducting such supervision as explained in the framework of agency theory. For the next researchers who are interested in doing further study can add other variables that may affect the practice of income smoothing such as the presence of family ownership in the company, the year of observation, and so-forth.

**REFERENCES**


*Institutional Ownership, Types of Industry,...*


IDX (The Indonesian Stock Exchange). 2016. www.idx.go.id


