STUDYING THE RELATIONSHIP BETWEEN FREE CASH FLOWS AND PERFORMANCE PREDICTION IN THE CORPORATIONS OF ACCEPTED IN TEHRAN STOCK EXCHANGE

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Abstract: Free cash flows is a benchmark for measuring the performance of companies and shows the cash available to the company after it has incurred expenses for maintaining or developing assets. Firms with positive free cash flows have high performance, so management tends to cut down profits slowly due to political costs. Because the high performance of the company attracts the attention of the public institutions (the tax office), they are trying to reduce or conceal their high performance using profit management. But companies with negative cash flows are incapable of supporting the growth of profit and income. An inadequate free cash flow could force the company to increase its debt level. Therefore, the management tends to perform better with increasing profit management. The main purpose of this study is to study the relationship between free cash flows and performance prediction in companies listed in Tehran Stock Exchange. For this purpose, the financial information of 102 companies listed in Tehran stock exchange were used during 2011-2015. The results of the research show that there is a significant relationship between free cash flow, return on assets and return on equity and future value of the company.

Keywords: free cash flows, performance prediction, Financial Leverage, Companies of accepted in Tehran Stock Exchange

1. INTRODUCTION

Today, due to the expansion of economic activities, financial markets and the prosperity of investing in equity markets, especially stock exchanges by natural and legal persons, access to accurate and timely information and their accurate and realistic analysis is the most important tool for making the right decisions and acquiring Expected benefit and optimal use of financial resources. In today's society, information plays an important role in human life, and the more advanced the community uses the more and better information. Advancement in the developed communities is an effective and efficient use of information.

The final product of the accounting process is to provide information to various users, both domestic and outside users, in the form of accounting reports. The group of accounting reports designed to provide information needs of non-company users is included in the field of financial accounting. The comprehensive research and analysis of the securities markets and the correct conclusion can realize the speed of growth in these markets. Reputable scholars of the world have shown that they are successful in securing and capitalizing, and this is the result of shareholders' trust in capital markets and market efficiencies, so that they are sure that their investments are not wasted and bring in reasonable gains. Investigating various categories affecting the stock market can help shareholders to make the right decisions, and the optimal allocation of economic resources is more desirable and investment is better (Ghaemi et al., 2003).

A number of financial researchers consider accounting to be an information system, and some think that the main objective of accounting is to provide useful information for decision making. It is the task of the researchers of this science to provide information so that decision makers can make the right decision based on them. In this research, we have been trying to pursue this goal.

2. RESEARCH PROBLEM

One of the important goals of financial reporting is to provide useful information for decision making. The users of accounting information, based on the reported financial statements, evaluate the profitability and forecast future cash flows of the company and then, by establishing a logical link between profitability and future cash flows, assess the company's value and decide on these predictions. (Cooper et al., 2004). The concept of open-loop positive cash flows indicates that the post-payment unit.

Expenditures and investments have surplus cash. In contrast, some companies may face negative cash flow. Negative free cash flow is not always bad and unfavorable, but its negative causes are important and should be analyzed. From the point of view of the stockholder of the business unit, free cash flows can be considered as a measure to create value for them. Because commercial entities with high positive cash flow are expected to invest in the new investment plans for their shareholders. Therefore, the purpose of this research is to examine the existence or non-existence of the relationship between free cash flows and the value created for shareholders. From an economic point of view, with the assumption of the logic of the behavior of individuals, it is assumed that everyone in the first place seeks to maximize their own interests.

Firms with positive free cash flows have high performance, so management tends to cut down profits slowly due to political costs. Because the high performance of the company attracts the attention of the public institutions (the tax office), they are trying to reduce or conceal their high performance using profit management. But companies with negative cash flows are incapable of supporting the growth of profit and income. An inadequate free cash flow could force the company to increase its debt level. Therefore, management tends to perform better with increased earnings management (Yodianti, 2008).

A review of the studies reveals different views on free cash flow and its calculation method. Jensen was one of the first to explain and define the theory of free cash flows. In Jensen's view, the cash flows of a cash-generating unit are cash surpluses that are required for all projects with a positive net present value (based on a discount on the cost of capital). Free cash flow is a benchmark for measuring companies' performance and cash flows that the company, after spending on it has authority. Open cash flow is important in that it allows the company to explore opportunities that increase shareholder value. Despite the papers and research conducted in the country about the prediction of the company's performance and its relationship with free cash flows has not been considered. This research is aimed at proving empirical strategies through the financial and internal environment of the company and exploring investment fundamentally.

3. RESEARCH BACKGROUND

Marzieh Fereydouni et al. (2012) examined the effects of free cash flows and agency costs on the performance of listed companies in Tehran Stock Exchange. The results of the statistical analysis of the research hypotheses show that there is a positive and significant relationship between free cash flows and asset turnover ratio (reversal of agency costs). Also, there was a negative and significant relationship between free cash flow and operating profit

fluctuations and net profit fluctuations. In addition, the research findings indicate that free cash flows has a positive and significant relationship with firm performance. Therefore, the present study obtained some evidence regarding the violation of the cash flows hypothesis. However, there was no significant relationship between agency costs and performance in order to confirm the agency's theory in Tehran Stock Exchange.

Salehi Kahrizzangi and others (2012) examined the effect of free cash flows and cost of representation on the performance of business units. The results of the research show that free cash flows has a positive effect on equity returns, while free cash flows has no effect on return on assets and there is no significant relationship between these two variables. In addition, the results indicate that free cash flows has a negative effect on the Q Tobin Index and stock returns. The results also show that the cost of representation is positively affected by equity returns, return on assets, Tobin Q index and stock returns.

The findings of Singer and et al (2010) show that there is no relation between cash flows from operating activities and stock trading, but there is a positive and weak correlation between changes in receivables and changes in payables with stock returns.

The research results of Hooshyaripour (2011) show that operating profit has an impact on stock returns, while free cash flows have no effect on stock returns and there is no significant relationship between these two variables. In addition, the results indicate that with the addition of free cash flows to the model, a significant relationship between operating profit and stock returns persists. In other words, free cash flows do not affect the relationship between operating profit and stock returns.

The results of the statistical analysis of the research hypotheses, Mahmoud Abadi and colleagues (2014), show that free cash flows has a positive and significant relationship with all the criteria for evaluating the performance of the company. Therefore, the present study obtained some evidence of a violation of the hypothesis of free cash flows. However, there was no significant relationship between representation and performance costs in order to confirm the representation theory in Tehran Stock Exchange.

The results of Javadi and Hashemi's research (2015) show that there is a direct and significant relationship between the free cash flows of firms with their actual value. The real value of firms is more than their projected value in the market, and the estimated value of firms based on free cash flow is higher than their market value.

Findings of Yousefi's research (2016) show that free flows of cash has a significant effect on the synchronization of stock returns of companies, but the growth of companies does not have a moderating effect on the relationship between free cash flows and the synergy of return on equity. This finding shows that free cash flows can range from 25% of the change in stock behavior.

The results of Khodadi et al. (2016) showed that the free cash flows of companies with a higher percentage of management ownership and higher financial leverage is less than the free cash flows of other companies. However, the results of the research for the impact of the quality of profit and the amount of institutional ownership on the valuation of the free cash flows of listed companies in Tehran Stock Exchange did not apply.

Rahman et al. (2012) also evaluated the effect of intellectual capital components on the performance of Pakistani banks. The results of this research show a positive and significant relationship between human capital and structural capital with return on assets and equity returns. The results of this research also show a positive and significant relationship between physical capital and equity returns.

Eudentity (2008), in a study using 150 sample companies, examines the effect of earnings management on the relationship between free cash flows and stockholder value. The results of the research show that with 95% confidence, changes in free cash flows are related to changes in shareholders' wealth. In this research, he also showed that there is a significant direct relation between free cash flows and shareholders 'equity, but there is no significant direct relation between cash flows and shareholders' equity. In the second hypothesis test, he concludes that with 99 percent confidence, profit management at the whole sample level and at the level of positive cash flows would weaken the relation of cash flows to wealth created for shareholders.

Reina et al. (2009), in a study entitled "Free-flow Cash flows, Profit Management and Audit Committee," highlighted how much free-market cash surplus was related to profit management. In this study, it is assumed that directors of companies that have high free cash flows have good operating profits in the administration of profits. The results of the research show that the independent audit committee helps companies with free cash flows monitor their profit management practices.

Neon (2013) reviewed the cash flows and the power of predicting the performance of electric companies. The results of his research show that free cash flows have a significant relationship with operating cash flows and net profit. But there is no significant relationship between predictive power. In addition, research shows that there is a relationship between free cash flow and customer satisfaction.

Hejazi and Bahtati Zashtani (2014) show that free cash flows representation costs have a significant and

positive effect on the distribution of profits and financial leverage. In addition, the size and profitability have a positive and significant effect on the division of profits.

The results of Najmi et al. (2015) show that there is a significant relationship between equity ratio of a company and its performance. Also, there is a significant relationship between debt ratio (capital structure) and performance, and between free cash flows and firm performance.

The results of Nakhai and Jafari (2015) show that there is an inverse relationship between capital structure and financial performance measurement criteria (return on assets, annual returns, and economic value added). But there is a direct and significant relationship between free cash flows and financial performance evaluation criteria (asset return, annual returns, and economic value added).

4. RESEARCH OBJECTIVE

Study of the relationship between free cash flows and performance prediction in listed companies in Tehran Stock Exchange

5. RESEARCH QUSTIONS

Is there a significant relationship between free cash flow and future performance (return on equity)?

Is there a significant relationship between free cash flow and future performance (return on equity)? Is there a significant relationship between free cash flow and future performance (company value)?

6. RESEARCH HYPOTHESES

There is a significant relationship between free cash flow and future performance (stock returns).

There is a significant relationship between free cash flow and future performance (return on equity).

There is a significant relationship between free cash flow and future performance (company value).

7. RESEARCH METHODOLOGY

This research is based on the deductive-inductive reasoning and, in terms of method, a descriptive research based on the actual information contained in the financial statements of the companies, it is also considered as an applied research in terms of purpose. The required information in this study was gathered from the New Way Software and the reports published by the Securities and Exchange Organization. Also, for analyzing data, Excel and

Eviews software will be based on the combined data analysis.

7.1. Statistical Population

The statistical population of this research includes companies listed on Tehran Stock Exchange which have the following conditions:
1. During the period under review, there is no change in the financial period.
2. Investment companies, financial intermediaries, and the Welsh Bank.
3. The data they are looking for are available. Finally, for data extraction, according to the correct sampling method, a statistical sample is selected from this population

8. RESEARCH FINDINGS

8.1. Testing the model of research Hypotheses

$$R_{t+1} = b_0 + b_1 FCF_t + b_2 \text{ Control variable } t + e_t,$$

$$(1)$$

Where in:
Annual Corporate Income (Corporate Performance Criteria)
FCF Free Cash Flow

$$Roa_{t+1} = b_0 + b_1 FCF_t + b_2 \text{ Control variable } t + e_t,$$
$$(2)$$

We have:
Roa Return on equity (corporate performance benchmark)
$$Q_{t+1} = b_0 + b_1 FCF_t + b_2 \text{ Control variable } t + e_t,$$
$$(3)$$

We have:
Q: QT Tobin, company value (corporate performance benchmark)
Control variables
LTD Debt to total assets (financial leverage)
TOTSALE logarithms of total sales (company size)

8.2. Estimation of research model and hypothesis testing

In this part of the research, according to the tests carried out and also the analysis of the variance of the variance for the research model and the determination of the estimation method, we will estimate the model and test the hypotheses of the research.

8.3. Model estimation results and hypothesis testing

Estimates of the first model of research

Table 1: Results from the first model

significance level	StatisticsT	Standard deviation	Variable coefficient	Variable
$Rit+1 = b0 + b1\ FCFit + b2\ Control\ variableit + eit$				
0/000	-7/75	0/56	-4/34	Free cash flows
0/000	4/19	0/93	3/90	Financial Leverage
0/54	20/60	0/61	0/37	power of the company
0/000	16/7813	0/4170	6/9986	Intercept
0/033				R2
0/027				Justified R2
5/18				F
0/000				Prob
1/98				Durbin-Watson statistics

8.4. The result of the first model of research

The F statistics shows that overall significant of model coefficients and Durbin Watson statistics with 1.99 which shows there is no self-correlation in among of the components of the disturbance. The coefficient of determination and the modified coefficient of determination of the above model are 3.37% and 2.79%, respectively. Therefore, it can be concluded that in the regression equation only about 2.79% of the dependent variable variations by independent and control variables are explained.

8.5. The result of the first hypothesis

Independent variable of free cash flows is negative and with respect to the level of 0/000 (less than the estimated level of error 5 hundredth), there is a significant reverse relationship with future return on equity.

The controller variable is positive for the company size, but with a significant level of 0.54 (more than the estimated level of error of 0.005), there is no significant relationship with future return on equity.

The financial leverage control coefficient is positive and with respect to the level of 0/000 (less than the estimated level of error of 0.005), there is a significant and direct relation with future return on equity.

Table 2: Results from the second model

significance level	StatisticsT	Standard deviation	Variable coefficient	Variable
$Roe+1 = b0 + b1\ FCFit + b2\ Control\ variableit + eit$				
0/01	2/42	0/12	0/29	Free cash flows
0/60	0/52	0/08	0/04	Financial Leverage
0/12	-1/55	0/07	-0/11	Company Size
0/01	2/45	0/43	1/05	Intercept
0/87				R2
0/83				Justified R2
26/34				F
0/000				Prob
1/99				Durbin-Watson statistics

8.6. The result of the second model of research

The F statistics shows that overall significant of model coefficients and Durbin Watson statistics with 1.99 which shows there is no self-correlation in among of the components of the disturbance. The coefficient of determination and the modified coefficient of determination of the above model are 87% and 83%, respectively. Therefore, it can be concluded that in the regression equation only about 83% of the dependent variable variations by independent and control variables are explained.

8.7. The result of the second hypothesis

Coefficient of Independent variable of free cash flows is positive and with considering the significant level of 0/01 (less than the estimated error level of 0.005), there is a significant and direct relationship with future return on equity. Coefficient of control variable of company size is negative and financial leverage is positive, but with according to the significant level of 0.60 and 0.12 (more than the estimated level of error of 0.005), there is no significant relationship with Future return on equity.

Table 3: Results from the third model

significance level	StatisticsT	Standard deviation	Variable coefficient	Variable
$Q+1 = b0 + b1\ FCFit + b2\ Control\ variableit + eit$				

0/04	-2/03	0/42	-0/85	Free cash flows
0/73	0/33	0/68	0/23	Financial Leverage
0/000	-5/33	0/32	-1/73	Company Size
0/000	6/37	2/11	13/47	Intercept
0/58				R2
0/47				Justified R2
5/31				F
0/000				Prob
2/42				Durbin-Watson statistics

8.8. The result of the third model of research

The F statistics shows that overall significant of model coefficients and Durbin Watson statistics with 2.42 which shows there is no self-correlation in among of the components of the disturbance. The coefficient of determination and the modified coefficient of determination of the above model are 57% and 47%, respectively. Therefore, it can be concluded that in the regression equation only about 47% of the dependent variable variations by independent and control variables are explained.

Coefficient of Independent variable of free cash flows is negative and with considering the significant level of 0/04 (less than the estimated error level of 0.005), there is a reserve relationship with future return on equity.

Coefficient of control variable of company size is negative and with according to the significant level of 0.000 (less than the estimated level of error of 0.005), there is a significant relationship with Future return on equity.

Coefficient of control variable of financial leverage is positive, but with according to the significant level of 0.73 (more than the estimated level of error of 0.005), there is no a significant relationship with Future return on equity.

9. CONCLUSION

The present study is based on the data of 102 firms listed in Tehran Stock Exchange during 2011-2015. Using multiple regression, a model is proposed to illustrate the individual's judgment in predicting future performance. The findings of this study are as follows:

Table 4: Results of Testing

Results of Testing	Type of Relationship	Confidence Level	Hypotheses
Confirmation of hypothesis	Negative	95percent	Between free cash flow and future performance (return on equity) there is a significant relationship.
Confirmation of hypothesis	Positive	95percent	Between free cash flow and future performance (return on equity) there is a significant relationship.
Confirmation of hypothesis	Negative	95percent	There is a significant relationship between free cash flow and future performance (company value).

The hypothesis is confidence level of the relationship of the test result. There is a significant relationship between free cash flows and future performance (stock returns). 95% negative confirmation of hypothesis

There is a significant relationship between free cash flows and future performance (return on equity). 95% positive confirmation of hypothesis

There is a significant relationship between free cash flows and future performance (company value). 95% negative confirmation of hypothesis

The hypothesis is the hypothesis of the confidence level of the relationship of the test result

There is a significant relationship between free cash flows and future performance (stock returns). 95% negative confirmation of hypothesis

There is a significant relationship between free cash flows and future performance (return on equity). 95%

positive   confirmation   of   hypothesis

There is a significant relationship between free cash flows and future performance (company value). 95% negative confirmation of hypothesis.

The results of the following investigations are consistent with the present study: Neon (2013) examined the free cash flows and the power of predicting the performance of electric companies. The results of his research show that free cash flows have a significant relationship with operating cash flows and net profit. But there is no significant relationship between predictive powers. In addition, research shows that there is a relationship between free cash flow and customer satisfaction.

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Salehi Kahrizzangi and others (2012) examined the effect of free cash flows and the cost of representation on the performance of business units. The results of the research show that free cash flow has a positive effect on equity returns, while free cash flows has no effect on return on assets and there is no significant relationship between these two variables. In addition, the results indicate that free cash flows has a negative effect on the Q Tobin Index and stock returns. The results also show that the cost of representation is positively affected by equity returns, return on assets, Tobin Q index and stock returns.

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