

THE INFLUENCE OF PROFITABILITY AND LEVERAGE ON FIRM VALUE (AN EMPIRICAL STUDY ON MANUFACTURING COMPANIES LISTED ON INDONESIA STOCK EXCHANGE FROM 2020 TO 2023)

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Abstract

This study aims to analyze the influence of profitability and leverage on firm value.

Profitability is measured using Return on Assets (ROA), while leverage is measured using Debt to Equity Ratio (DER). Firm value is assessed using Price to Book Value (PBV). The data used in this study are secondary data from the financial statements of companies listed on the Indonesia Stock Exchange (IDX) during the period 2020-2023. Data analysis is conducted using multiple linear regression. The results show that both profitability and leverage have a positive and significant influence on firm value. These findings indicate that increases in profitability and leverage can enhance firm value. The implications of this study highlight the importance for company management to consider profitability and leverage levels as key factors in efforts to increase firm value.

INTRODUCTION

In the era of globalization and rapid technological advancements, competition in the business world has become increasingly fierce. Companies are required not only to survive but also to thrive in the midst of dynamic market changes. To remain competitive, businesses must continuously enhance their firm value, an important indicator of operational and managerial success. Firm value reflects a company's performance, which is mirrored by stock prices shaped by market demand and supply, representing the public's real-time assessment of the company (Harmono, 2017). Two key factors that influence firm value are profitability and leverage. Profitability, as described by (Sutrisno, 2009), is a company's ability to generate profit from its operations. High profitability indicates that a company can generate substantial profits with operational efficiency, making it attractive to investors. Common measures of profitability include Return on Assets (ROA) and Return on Equity (ROE). On the other hand, leverage refers to a company's use of debt relative to its equity (Harahap, 2013). While leverage can boost profitability through tax advantages and lower capital costs, excessive leverage increases the risk

of bankruptcy if debt obligations cannot be met. Debt to Equity Ratio (DER) and Debt to Asset Ratio (DAR) are often used to assess a company's financial risk.

However, the relationship between profitability, leverage, and firm value is not always straightforward. Various internal and external factors, such as macroeconomic conditions, government policies, and market sentiment, can influence how these variables affect firm value. In Indonesia, empirical studies have yielded mixed results regarding the impact of profitability and leverage on firm value, particularly in capital-intensive industries like manufacturing. This research aims to further analyze the influence of profitability and leverage on firm value among manufacturing companies listed on the Indonesia Stock Exchange (IDX) from 2020 to 2023. By examining this relationship, the study seeks to provide valuable insights for both investors in making informed decisions and corporate management in devising optimal financial strategies. This period, which includes the economic downturn caused by the COVID-19 pandemic, presents a unique context to explore how profitability and leverage interacted with firm value under extreme economic conditions.

Based on the background of the problem that has been stated, the author identifies the problem in this research as probability and leverage effect on firm-value which influence is not yet certain, thus the following problems can be identified: (1) Unclear relationship between profitability and firm value: Although high profitability generally indicates good financial health, the specific impact of profitability on firm value, especially in the manufacturing sector in Indonesia, requires further investigation, (2) Ambiguous effect of leverage on firm value: While leverage can increase profitability through tax benefits, excessive leverage poses financial risks. The specific influence of leverage on firm value, particularly in the context of Indonesian manufacturing companies, is not well understood, (3) Mixed empirical findings on the relationship between profitability, leverage, and firm value: Previous studies in Indonesia have produced varying results regarding how profitability and leverage affect firm value, suggesting a need for more focused research in this area.

Based on the identification of this problem, the research questions that can be formulated as follows: (1) Does Profitability Affect Firm-value?, (2) Does Leverage Affect Firm-value?, (3) Do Profitability and Leverage, Simultaneously Affect Firm-value? The objectives of this research are as follows: (1) To determine the influence of profitability on firm value in manufacturing companies listed on the Indonesia Stock Exchange, (2) To determine the effect of leverage on firm value in manufacturing companies listed on the Indonesia Stock Exchange, (3) To determine the simultaneous effect of profitability and leverage on firm value in manufacturing companies listed on the Indonesia Stock Exchange.

LITERATURE REVIEW

Grand Theory

The Grand Theory used in this research is Signaling Theory. Signaling theory according to (Spencer, 1973) stated that:

Signals are actions taken by companies to indicate to investors the management's view of the company's processes. These signals are in the form of information regarding the steps that have been taken by management to realize the desires of the company's owners. The information provided by the company is very important because it influences the investment decisions of external parties. This information is crucial for investors and business actors because it essentially provides descriptions, records, or insights about the company's past, present, and future conditions, as well as their impact on the company's sustainability.

Definition Financial Statement

According to (Prihadi, 2020) states that:

Financial statement are the result of recording all financial transactions in the company.

Definition Financial Statement Analysis

According to (Munawir, 2010:35) states that:

Financial statement analysis is the analysis of financial statements that involves examining or studying the relationships and trends to determine the financial position, operating results, and the development of the company in question.

Definition Profitability

According to (Septiana, 2019) states that:

Profitability is a ratio aimed at determining the company's ability to generate profits over a certain period.

Definition Return On Assets (ROA)

According to (Adnyana, 2020) states that:

Return on Assets (ROA) describes the turnover of assets, measured by sales.

Definition Leverage

According to (Gusnandar et al., 2024) states that:

Leverage is the use of assets and sources of funds by a company that have fixed costs (fixed expenses) with the aim of increasing the potential profits for shareholders.

Definition Debt to Equity Ratio (DER)

According to (Sukamulja, 2019) states that:

Debt to Equity Ratio measures the percentage of liabilities in a company's capital structure. This ratio is important for assessing business risk, which increases as the amount of liabilities grows.

Definition Firm Value

According to (Pambudi et al., 2022) states that:

Firm value is the process a company has undergone to shape public perception of the company. A high firm value indicates that the company has good performance and its future prospects are trusted by investors

Definition Price to Book Value (PBV)

According to (Sugiono & Untung, 2016:71) states that:

Price to Book Value (PBV) is the comparison between the stock price and the book value of a company. A company with good management is expected to have a PBV of at least 1 or above the book value (overvalued).

Research paradigm

Based on the description above, the Research Framework can be described which can be seen in Figure 2.1 as follows:

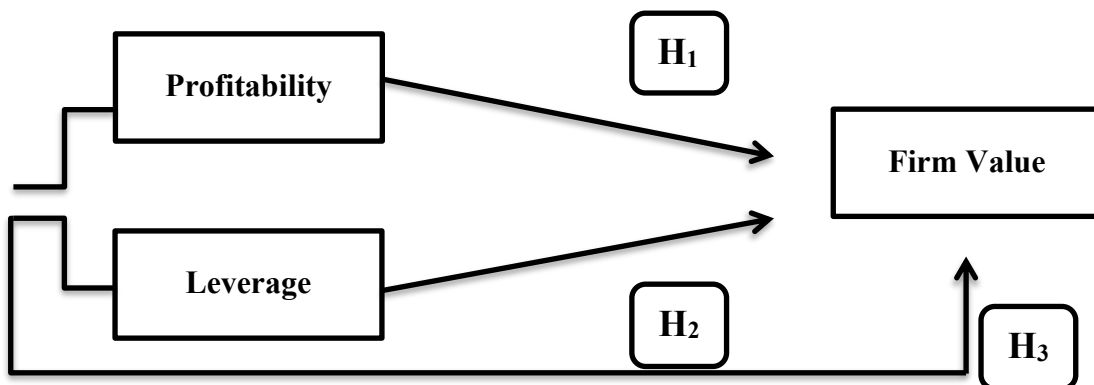


Figure 2.1

Research Framework

Source: Processed Data (2024)

A hypothesis is a temporary answer to a research problem formulation, which theoretically is considered the most likely or has the highest level of truth. According to (Sugiyono, 2019), a hypothesis is a temporary answer to a research problem formulation that has been stated in the form of a question sentence. Based on the problem formulation above, the hypothesis proposed is as follows:

H1: Profitability levels have an impact on Firm Value

H2: Leverage levels have an impact on Firm Value

H3: Profitability levels and Leverage levels simultaneously have an impact on Firm Value

RESEARCH METHODS

Types of Research and Research Objects

The research method used by the author is quantitative research method. Quantitative research is research by obtaining data in the form of numbers and analyzing it using statistics. The place for carrying out this research is at the Indonesia Stock Exchange Website. This research was conducted from July 2024 until completion.

Operationalization of variables

According to (Nurdin et al., 2019) states that:

Variables are operationalized based on the observed characteristics, allowing researchers to conduct careful observations or measurements of an object or phenomenon. The operationalization of variables is designed to facilitate data collection, prevent differing interpretations, and limit the scope of the variables.

The operationalization of variables in this research can be seen in the following table 3.1:

Variable	Definition	Indicators	Formula
Profitability	Profitability is a ratio aimed at determining the company's ability to generate profits over a certain period.	Return on Assets (ROA)	$ROA = \frac{Net\ Profit}{Total\ Assets}$

Leverage	Leverage is the use of assets and sources of funds by a company that have fixed costs (fixed expenses) with the aim of increasing the potential profits for shareholders.	Debt to Equity Ratio (DER)	$DER = \frac{\textit{Total Liabilities}}{\textit{Total Equity}}$
Firm Value	Firm value is the process a company has undergone to Shape public perception of the company. A high firm value indicates that the company has good performance, and its future prospects are trusted by investors.	Price to Book Value (PBV)	$PBV = \frac{\textit{Market price per share}}{\textit{book price per share}}$

Population and Sample

The population in this study consists of all manufacturing companies listed on the Indonesia Stock Exchange during the period from 2020 to 2023. The objects to be researched include data such as the company's financial ratios and the values from the financial statements of companies listed on the IDX for the period of 2020 to 2023. The sample selection technique used is the systematic random sampling method, namely The initial selection of companies for the study was conducted randomly, followed by systematic sampling to avoid extreme or invalid company data.

The sample in this study can be seen in Table 3.2.

Stock Code	Sample of Companies
AKKU	PT Anugerah Kagum Karya Utama Tbk
ALDO	PT Alkindo Naratama Tbk
ASII	PT Astra International Tbk
AUTO	PT Astra Otoparts Tbk

BOLT	PT Garuda Metalindo Tbk
BUDI	PT Budi Starch & Sweetener Tbk
CAKK	PT Cahayaputra Asa Keramik Tbk
CEKA	PT Wilmar Cahaya Indonesia Tbk
COCO	PT Wahana Interfood Nusantara Tbk
FOOD	PT Sentra Food Indonesia Tbk
GDST	PT Gunawan Dianjaya Steel Tbk
GGRM	PT Gudang Garam Tbk
ICBP	PT Indofood CBP Sukses Makmur Tbk
IGAR	PT Champion Pacific Indonesia Tbk
IKAN	PT Era Mandiricemerlang Tbk
INCI	PT Intanwijaya Internasional
ISSP	PT Steel Pipe Industry of Indonesia Tbk
ITIC	PT Indonesian Tobacco Tbk
JPFA	PT Japfa Comfeed Indonesia Tbk
STAR	PT Buana Artha Anugerah Tbk
KAEF	PT Kimia Farma Tbk
LION	PT Lion Metal Works Tbk
MOLI	PT Madusari Murni Indah Tbk
MYOR	PT Mayora Indah Tbk

ROTI	PT Nippon Indosari Corpindo Tbk
SKBM	PT Sekar Bumi Tbk
SRSN	PT Indo Acidatama Tbk
TALF	PT Tunas Alfin Tbk
TOTO	PT Surya Toto Indonesia Tbk
VOKS	PT Voksel Electric Tbk

Table 3.2
Samples

Source: Processed Data (2024)

Data Sources and Collection

The type of data used is secondary data (financial statement) as main data and secondary data as supporting data.

Data analysis technique

The data analysis techniques used in this research are descriptive statistics, classical assumption tests, multiple linear regression analysis, and hypothesis testing using SPSS 26 software.

RESULTS AND DISCUSSION

The results of data processing and analysis conducted in the previous tests show that profitability (measured by ROA) has a significant effect on firm value (measured by PBV).

In studies conducted before the COVID-19 pandemic, nearly all indicated that profitability, as measured by ROA, positively impacted firm value. For instance, research

by Hafiz & Vina (2022) found a positive and significant influence of profitability on firm value in the food and beverage sector for the period 2018-2019. It is clear from this comparison that profitability had the same impact on business value both before and after the COVID-19 pandemic. The current study and previous studies both show that profitability significantly and favorably affects firm value. Processing and analyzing the data from earlier studies has shown that leverage, as determined by the Debt to Equity Ratio (DER), significantly affects firm value, which is determined by the Price to Book Value (PBV).

In studies conducted before the COVID-19 pandemic, nearly all indicated that leverage did not affect firm value. For instance, Lamba & Atahau (2022) found that the level of leverage in manufacturing companies listed on the IDX from 2017 to 2020 did not influence firm value, suggesting these companies relied more on internal financing from retained earnings rather than external debt. Similarly, research by Rizki et al. (2022) on food and beverage companies from 2018 to 2020 showed that increased debt usage did not impact firm value, indicating that companies using no debt at all were not significantly different from those fully financed by debt.

Comparing the findings from previous research with this study reveals a shift: prior to COVID-19, leverage was not seen as affecting firm value, whereas post-pandemic studies indicate it does.

This shift may be due to manufacturing companies increasingly relying on debt for financing during the pandemic, as they struggled to utilize their own capital amid the economic downturn in Indonesia.

The results of previous data processing and analysis show that profitability (measured by Return on Assets, ROA) and leverage (measured by Debt to Equity Ratio, DER) significantly influence firm value (measured by Price to Book Value, PBV) simultaneously.

Research before the COVID-19 pandemic, such as Joko Riyadi (2019), confirmed that both ROA and DER together impact PBV. Studies conducted after the pandemic showed similar findings, indicating consistency in results across both periods.

A high ROA indicates strong financial performance and efficiency in asset utilization, which boosts investor confidence and demand for shares, ultimately raising the PBV.

Conversely, a well-managed high DER can enhance firm value if debt is used effectively for growth, making investors view it as a tool for increasing firm value.

Overall, optimal management of profitability and leverage positively impacts firm value. High profitability lays a strong foundation for growth, while effective leverage provides additional resources to maximize this potential, leading to an increase in PBV.

CONCLUSION

Based on the research results, it shows that High profitability, as indicated by a high Return on Assets (ROA), demonstrates strong financial performance and efficiency in asset utilization. This leads to increased investor confidence and demand for shares, ultimately enhancing the firm's value as reflected in a higher Price to Book Value (PBV).

Based on the research results, it shows that Effective leverage, represented by a high Debt to Equity Ratio (DER), can positively influence firm value when debt is strategically used for growth and expansion. When managed well, leverage serves as a tool for increasing the firm's value, contributing to a higher PBV.

SUGGESTION

In making investment decisions on the Indonesia Stock Exchange (BEI), investors should consider profitability and leverage as key factors influencing firm value, particularly the Price to Book Value (PBV). This research demonstrates that both profitability and leverage significantly impact firm value. It is hoped that this study will encourage investors to assess investment risks by comparing indicators such as profitability and leverage, leading to more informed investment choices.

The research offers significant perspectives to the management of the company on how to improve the firm's value and draw in investors. To increase profitability and leverage, management should review and realign business plans. This will increase firm value. An increased firm value will pique investors' interest in funding the business.

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