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ENHANCING COMPANY VALUE THROUGH PROFITABILITY MEDIATION (A STUDY ON MANUFACTURING COMPANIES LISTED ON THE INDONESIA STOCK EXCHANGE DURING THE PERIOD OF 2018-2021)

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Abstract

The research is based on the fact that there is a significant fluctuation in the performance of companies listed on the Indonesia Stock Exchange, leading to the emergence of a phenomenon known as the 'gap' phenomenon. The gap phenomenon is characterized by the inconsistency in the influence of variables such as ROE, capital expenditure, and tangible assets on profitability and their impact on company value. The objective of this study is to analyze the influence of the variables ROE, capital expenditure, and tangible assets on profitability and their impact on company value in the manufacturing industry listed on the IDX during the period from 2018 to 2021. The population in this study consists of all manufacturing companies listed on the Indonesia Stock Exchange during the period from 2018 to 2021. The research analysis method used in this study is Smart PLS.

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INTRODUCTION

This research examines the value of a company with the rationale that the goal of a company is the prosperity of its shareholders. A high company value reflects the prosperity of shareholders, where the higher the company's value, the higher the price willing to be paid when the company is sold. Profitability is used as an intervening variable because profitability is not the company's goal; the company's goal is the prosperity of shareholders. It is about how the company can thrive by providing value to itself in delivering shareholder prosperity. The company requires proper investment management in the form of good performance to obtain a profitable company value.

The use of ROA as an intervening variable is supported by previous research (5) that examined the impact of ROE on firm value through mediating variables. (20) concluded that Tobin's Q can be used as a measure to determine a firm's value. The rationale for using Tobin's Q aligns with the philosophy of firm value, indicating the price investors are willing to pay when the company is sold. Tobin's Q measures the ratio of market value to total assets owned by the company, and the larger Tobin's Q, the higher the market values the firm. Manufacturing companies were chosen as the population in this study because the manufacturing industry has the highest number of companies compared to other industries listed on the IDX (Indonesia Stock Exchange), and it is also the sector with the largest trading activity in terms of stock. Therefore, due to its significant presence, it is expected that manufacturing companies have a substantial impact on the dynamics of stock trading on the stock exchange. (24) stated that profitability fluctuations are relatively small, but there are issues with the movement of ratios that affect profitability, which do not align with the movement of profitability itself.

This research is motivated by the research gap in previous studies on firm value. Based on research conducted by (Budi Astuti and Putu Yadnya, 2019), profitability has a t-value of 2.821 and a sig. value of 0.009, indicating that the independent variable profitability has a significant positive impact on firm value individually, and the first hypothesis (H1) is accepted. Then, in a study conducted by (Diah Novita and Ayu, 2019), profitability has a coefficient of 0.899 and a Sig. value of 0.000, stating that a 1 percent increase in profitability leads to a positive impact on firm value. In another study (2), profitability has a prob t-value of 0.000 < 0.05, indicating that profitability has a significant influence on firm value. In a study conducted by (25), it is found that the t-value for firm size is 1.729 with a sig. value of 0.005, meaning that firm size has a simultaneous positive effect on the independent variable, which is firm value. In another study (2), the firm size variable has a prob t-value of 0.000, meaning that firm size, in partial terms, has an influence on firm value.

Hypotheses Development

The problem-solving approach in this research involves hypothesis testing to analyze the relationships between variables. Capital expenditure represents the spending of money for long-term capital financing. This expenditure includes various costs such as the purchase of fixed assets, waste management expenses, promotional expenses, and research costs. Capital expenditure falls under the realm of investment policy and is directed towards the development or expansion of business to ensure the company's continued existence in the face of competition. (20) states that capital expenditure has a positive impact on profitability. Policies related to capital expenditure are closely linked to funding policies, and the success of this program greatly supports the success of funding selection programs. This policy aligns with the balancing theory, meaning that funding policies for capital expenditure are allowed as long as the costs incurred are below the level of profits obtained. (7) also states that capital expenditure has a positive impact on profitability.

H_1 = Capital expenditure has a positive impact on profitability.

The allocation of funds to finance this investment is part of capital expenditure, the benefits of which will only be realized after several years. Regardless of the source of funds used to finance this capital expenditure, choosing an investment implies an expectation of increasing the owner's wealth. This is because the selected investment yields a positive NPV (Net Present Value), and the larger the NPV, the greater the wealth addition for the owners. The relationship between capital expenditure and firm value is supported by Valuation Theory, where significant capital expenditure adds value to the company in the future, and is justified by previous research conducted by (20)(18).

H_2 = Capital expenditure has a positive impact on firm value.

Return On Equity (ROE) is a financial ratio related to profitability. This ratio is a component of balance sheet ratios and income statement ratios. ROE is used to measure a company's ability to generate profit based on its equity capital. The impact of profitability and liquidity ratios on profit growth in manufacturing companies. The results of this research indicate that ROA and ROE have a positive partial impact on profit growth (15).

H_3 = ROE has a positive impact on profitability.

The Return On Equity (ROE) ratio is the most important ratio, which can be calculated as net profit attributable to shareholders divided by total shareholders' equity. Shareholders certainly want to achieve a high return on their invested capital, and ROE reflects the level of return they obtain. If ROE is high, it will attract the interest of potential investors to invest, increasing demand for the stock, which in turn tends to raise the stock price and is also followed by an increase in the company's value. When there is an increase in profit, the stock price also rises, thereby increasing the company's value (17).

H_4 = ROE has a positive impact on firm value.

Assets represent the resources used for a company's operational activities. This research is supported by signaling theory, where a positive signal is conveyed by companies through a large amount of assets. Large tangible assets indicate that the company possesses significant physical assets, which have been efficiently managed, leading to higher profits (19). Based on the economic scale theory, which states that large tangible assets signify economic value for a company because they can serve as a strong capital guarantee for the company to achieve substantial profits (16).

H_5 = Tangible assets have a positive impact on profitability.

The magnitude of a company's assets can provide investors with important information about the company, which, in turn, fosters a high level of investor confidence and ultimately enhances the firm's value (16)(21). The larger the tangible assets, the more effectively the company utilizes its assets to generate total net sales. The more effectively a company uses its assets to generate net sales, the higher the value achieved by the company. (1) indicates that tangible assets have a positive impact on firm value. According to signaling theory, which suggests that large tangible assets send a positive signal for obtaining a high firm value.

H_6 = Tangible assets have a positive impact on firm value.

Profitability reflects a company's ability to generate profit by leveraging its total assets. A positive signal conveyed by a company through a high level of profitability adds value to the company. Profitable companies intentionally signal the market through information, and for this signal to be effective, it must be captured and well-perceived by the market and not easily imitated by lower-quality companies (14)(22). Companies with a high ability to generate profits through the utilization of their assets will have substantial cash reserves in the future. This will encourage the company to continue placing its funds in profitable investment positions in the future. The results of this research are empirically supported by (23), which indicates a positive impact on firm value. High profitability signifies a positive outlook for the company, prompting investors to respond positively to this signal, thereby increasing the firm's value. The positive impact of profitability on firm value can lead to positive sentiment among investors, driving up stock prices, which in turn increases the firm's value (4).

H_7 = Profitability has a positive impact on firm value.

To achieve profitability as expected, capital expenditure must be supported by effective asset management, including the management of related resources. This policy aims to expand business opportunities and is only justified if the company's performance, as reflected through profitability, is good (3). Large capital expenditure adds value to the company in the future, making investors more interested in buying the company's stocks, particularly when there is strong profitability.

H_8 = Profitability mediates the relationship between capital expenditure and firm value.

High profitability indicates a positive outlook for the company, prompting investors to respond positively to this signal and increasing the firm's value. The positive impact of profitability on firm value can lead to positive sentiment among investors, driving up stock prices. An increase in stock prices will also enhance the firm's value (8). A high ROE signals that the company has substantial additional earnings to add value to the company in the future, making investors more interested in buying the company's stocks, particularly when there is strong profitability.

H_9 = Profitability mediates the relationship between ROE and firm value.

Tangible assets are a ratio comparing fixed assets to total assets (6). The larger tangible assets indicate that with substantial assets, it can attract investor interest in investing. The more investors are interested, the easier it is for investors to obtain information about the company, which can increase the firm's value. High profitability signifies a positive outlook for the company, prompting investors to respond positively to this signal and increasing the firm's value. The positive impact of profitability on firm value can lead to positive sentiment among investors, driving up stock prices. An increase in stock prices will also enhance the firm's value (9). (13) demonstrates that tangible assets influence the magnitude of firm value, mediated by profitability.

H_{10} = Profitability mediates the relationship between tangible assets and firm value.

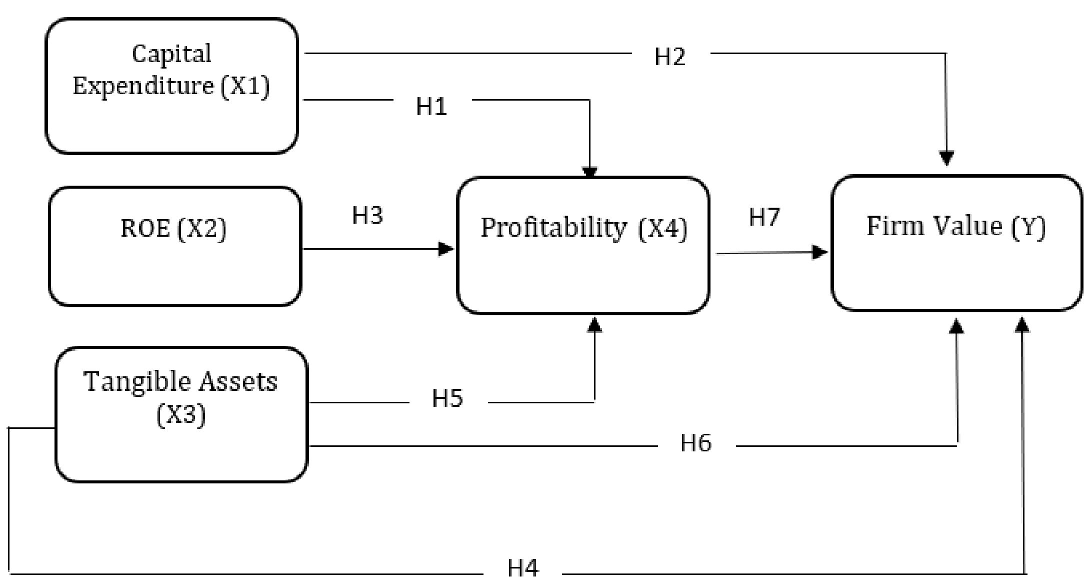

Figure 1. Research Model

METHOD

To analyze the influence of the independent variables on the dependent variable in the empirical research model, a multiple linear regression equation model is used. The multiple linear regression equation model is the most suitable model for analyzing this research model because it contains multiple independent and dependent variables, specifically, there are 3 dependent variables and 1 independent variables. Furthermore, to test the influence of intervening variables, the Path Analysis method is employed. Path Analysis is used to determine whether the independent variables have a direct or indirect effect on the dependent variable. The Smart PLS program is utilized to assist in analyzing the data used in the study. The type of data used is secondary data, which has been published by the Indonesia Stock Exchange from 2018 to 2021.

RESULT AND DISCUSSION

After conducting the analysis using Smart PLS, the results can be observed as follows:

Table 1. Outerloading Test

	Tangible Assets	Capital Expenditure	Firm Value	Profitability	ROE
TA 1	0.987				
TA 2	0.989				
TA 3	0.827				
TA 4	0.955				
CE 1		0.963			
CE 2		0.893			
CE 3		0.944			
CE 4		0.981			
FV 1			0.912		
FV 2			0.962		
FV 3			0.888		
FV 1				0.928	
PR 2				0.881	
PR 3				0.922	
PR 4				0.941	
PR 5				0.851	
RO 1					0.891
RO 2					0.988
RO 3					0.973
RO 4					0.972

From the results of the tightened outerloading test, it can be seen that some indicators have values below 0.7, so only indicators with values above 0.70 are used in this study. This is in line with Ghozali's (2016) recommendation, which states that the minimum requirement is 0.70. In Table 1, it can be seen that the indicators used already show values above 0.70, which means that these indicators can be used to measure this research model

The next step is to determine the lowest value of a variable and verify its reliability while simultaneously testing the validity of the relationship between indicators and latent constructs or variables. The calculation results are as follows:

Table 2. Reliability and Validity Test

	Cronbach's Alpha	rho_A	Composite Reliability	Average Variance Extracted (AVE)
Tangible Assets	0.97	1.043	0.969	0.887
Capital Expenditure	0.961	0.983	0.971	0.894
Firm Value	0.91	0.916	0.944	0.848
Profitability	0.945	0.949	0.958	0.82
ROE	0.969	0.969	0.977	0.915

Based on the previous calculations, it can be determined that all constructs have high reliability because the Composite Reliability values are > 0.70 and Cronbach's Alpha values are > 0.60. Since the average extracted variance values are > 0.50, it indicates validity. Therefore, it can be concluded that the validity has converged to the point where latent variables can explain more than half of the variance in the indicators on average (Ghozali, 2016).

Next is to test the hypotheses with path coefficients to determine the direction of relationships between variables. The calculation results are as follows:

Table 3. Hipotheses Test

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values
Tangible Assets → Firm Value	0.659	0.656	0.025	4.104	0.000
Tangible Assets → Profitability	-0.614	-0.679	0.023	4.592	0.000
Capital Expenditure → Firm Value	0.44	0.399	0.219	2.012	0.045
Capital Expenditure → Profitability	0.321	0.359	0.078	4.181	0.000
Profitability → Firm Value	1.011	0.976	0.443	2.282	0.023
ROE → Firm Value	0.225	0.238	0.074	2.562	0.003
ROE → Profitability	-0.643	-0.661	0.204	3.15	0.002

The direction and direct relationships between independent variables and dependent variables are shown in Table 3. It can be seen that the dependent variable influences the independent variable, as indicated by the P Values < 0.05. Table 3 also explains the direction of the relationship between the dependent variable and the independent variable. It is evident that the Tangible Assets and ROE variables have a negative direction of influence on the Profitability variable. This is indicated by the numbers in the Original Sample (O) column showing negative values. Meanwhile, the other dependent variables have a positive impact on both firm value and profitability.

Next is the result of hypothesis testing with the mediation of the profitability variable. The results are as follows:

Table 4. Hipotheses Test

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values
Tangible Assets → Profitability → Firm Value	-0.427	-0.491	0.013	4.259	0.000
Capital Expenditure → Profitability → Firm Value	0.144	0.157	0.039	2.812	0.005
ROE → Profitability → Firm Value	-0.135	-0.143	0.038	2.712	0.005

Table 4 shows the relationship between dependent variables and independent variables mediated by the profitability variable. It can be observed that Tangible Assets and ROE have a negative relationship with firm value through the profitability variable. Meanwhile, the Capital Expenditure variable has a positive relationship with firm value through the profitability variable. This is indicated by the numbers in the Original Sample (O) column, which display both positive and negative values.

CONCLUSION AND RECOMMENDATION

This research examines the influence of dependent variables on the increase in firm value with profitability as a mediator. The dependent variables used are Capital Expenditure, ROE, and Tangible Assets, ROE. From the results of the data analysis using Smart PLS, it can be observed that, Tangible Assets have a positive impact on Firm Value. This can be interpreted as an increase in Tangible Assets leading to an increase in Firm Value. Tangible Assets have a negative impact on Profitability. This can be interpreted as an increase in Tangible Assets leading to a decrease in Company Profitability. Capital Expenditure has a positive impact on Firm Value. This can be interpreted as an increase in Capital Expenditure leading to an increase in Firm Value. Capital Expenditure has a positive impact on Profitability. This can be interpreted as an increase in Capital Expenditure leading to an increase in Profitability. Profitability has a positive impact on Firm Value. This can be interpreted as an increase in Profitability leading to an increase in Firm Value. ROE has a positive impact on Firm Value. This can be interpreted as an increase in ROE leading to an increase in Firm Value. ROE has a negative impact on Firm Value. This can be interpreted as an increase in ROE leading to a decrease in Firm Value.

In addition to testing the dependent variables against the independent variables, this research also examines the relationship between dependent variables and independent variables with profitability as a mediator. Here are the test results obtained using Smart PLS. Tangible Assets have a negative impact on the Firm Value variable with Profitability as a mediator. This can be interpreted as, with the mediation of Profitability, an increase in Tangible Assets leads to a decrease in Firm Value. Capital Expenditure has a positive impact on the Firm Value variable with Profitability as a mediator. This can be interpreted as, with the mediation of Profitability, an increase in Capital Expenditure enhances Firm Value. ROE has a negative impact on the Firm Value variable with Profitability as a mediator. This can be interpreted as, with the mediation of Profitability, an increase in ROE reduces Firm Value.

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