The Influence of Capital Structure on Company Value with Financial Performance as a Mediation Variable

Retnoningrum Hidayah[1], Anas Tasya Givia Ratri[2]
{retnoningrum.hidayah@mail.unnes.ac.id[1], anasratri726@gmail.com[2]}

Universitas Negeri Semarang, Indonesia[1, 2]

Abstract. This study determines the effect of capital structure on company value with financial performance as a mediating variable. The declining value of Gross Domestic Product (GDP) indicates that the economic condition is not significant enough. This is a result of the level of investment that is still weak. To be able to increase the value of GDP, the enthusiasm of industry players must remain high and companies must be more competitive to increase the value of their companies. The population of this study was manufacturing companies from various industrial sectors listed on the Indonesia Stock Exchange from 2017-2020 and the selection of the company used the purposive sampling technique. Data analysis used descriptive statistical analysis and the Structural Equation Model with the help of SmartPLS 3.0. The results of this study showed that capital structure did not affect company value but influential financial performance. The financial performance had a positive effect on company value and able to mediate between capital structure and company value. For further research to add other indicators so that investors have more considerations so that their investment decisions are right.

Keywords: Capital Structure, Company Value, Financial Performance

1 Introduction

Indonesia's economic growth, which is indicated by the value of Gross Domestic Product (GDP), is decreasing. The declining value of GDP shows that the economic conditions in Indonesia have not been significant enough for the welfare of its people. This is partly due to the weak level of investment. To be able to increase the value of GDP, the enthusiasm of industry players must remain high in order to encourage the economy in Indonesia. With the enthusiasm of industry players will also increase investment activities so that companies will be more competitive to increase the value of the company. Investors must be more careful in giving their investment decisions so that they are not wrong in investing their capital. Company value as a description of a company that will show the level of prosperity of its shareholders. Company value is calculated using the Price Book Value (PBV) formula. Investors will find the right stock by seeing whether the stock is classified as expensive or cheap. High stock prices are usually caused by high investor demand. This indicates that the more investors who enter it will increase the value of the company. The theory that supports this research is agency theory by This indicates that the more investors who enter it will increase the value of the company. The theory that supports this research is agency theory by This indicates that the more investors who enter it will increase the value of the company. The

ICE-BEES 2022, August 09-10, Semarang, Indonesia

DOI 10.4108/eai.9-8-2022.2338670

theory that supports this research is agency theory by Jensen & Meckling [2] and signalling theory by Spence [3]. Agency theory is used to solve problems related to the principal and agent related to the separation of ownership which can lead to agency conflicts. Meanwhile, signalling theory is a form of signal/information that is conveyed in the financial statements provided by parties within the company to parties outside the company in order to see the condition of the company.

Investors before investing their capital also see first how the capital structure in a company and make it an indicator to see the high and low demand for its shares. Capital structure in increasing the value of a company becomes an important issue and becomes a debate in business activities, especially in the financial sector [4]. The capital structure is measured using the Debt-to-Equity Ratio (DER) formula where the amount of debt provided by creditors is divided by the company's equity. According to research results Utami [5] and Nguyen et al. [6] said that if the company calculates the capital structure using the capital owned by the company itself more than debt it will produce a positive effect on increasing the value of the company. The optimal capital structure will have a good influence on increasing the value of the company.

H1: Capital structure has a positive effect on company value

Taking funding sources will also affect the optimization of a capital structure. If the company is able to process its capital structure properly, it will affect the results of a company's financial performance. If you choose an inappropriate capital structure, the company must bear the risks that will arise in the future [7]. Based on research Meshack et al. [8] said that the capital structure affects financial performance.

H2: Capital structure has a positive effect on company value

Financial performance is an important indicator because it is used as a benchmark by investors to see the merits of a company or its financial position so that investors will consider more before investing their capital. Investors' assessment of financial performance is considered quite important and needed because by observing the resulting financial performance, you will see how the company's success has been achieved [9]. If the company's performance is good, it will affect the value of shares and shareholders. However, if the company's performance is poor, shareholders will think again to put their capital in the company and can even withdraw their share ownership in the company. Financial performance is measured using a profitability ratio, namely Return on Assets (ROA). ROA is measured by comparing net income after tax with total assets owned by the company, this will determine the company's ability to generate profits. Based on research Fadrul et al. [10] Good financial performance has an effect on increasing company value. Good performance is the result of management's work in managing company resources effectively and efficiently.

H3: Financial performance has a positive effect on company value

Mudany et al. [11] said that the selection of capital structure is the most important and even difficult business that must be carried out by the company's management. Investors after placing their funds will expect reciprocity from the company, namely the profits that will be obtained. Therefore, the management is required to manage the company well by choosing the optimal capital structure so as to produce good company financial performance as well. If the financial performance is good the result of choosing the optimal capital structure will increase the number of investors entering. The increasing number of investors results in an increase in the value of the company. So that financial performance is able to mediate the effect of capital structure on company value in accordance with the results of the study Yurianda & Masdupi [7].

H4: Financial Performance Is Able to Mediate Capital Structure on company value

2 Method

The type of research is quantitative research with secondary data sources. The research design is explanatory research with documentation data collection techniques. In addition, the data in this study are in the form of annual reports of various industrial sector companies in the 2017-2020 period and listed on the IDX which were taken through the website www.idx.co.id. The sample selection in this study used a purposive sampling technique where the sample selection technique was in accordance with the specified criteria where these criteria met the research interests. Based on the purposive sampling technique, 22 samples of companies met the criteria. The data analysis technique used is descriptive statistical analysis and Structural Equation Model [12]. The hypothesis testing tool in this study uses partial least squares and the Sobel test with the help of a statistical program, namely SmartPLS 3.

3 Result and Discussion

3.1 Outer model analysis

3.1.1 Convergent validity

The test requirements are if the correlation > 0,70 with the construct you want to measure, it is considered reliable and if the loading value is 0,5-0,6 then it is still acceptable for initial research [12].

Table 1. Convergent validity values

Indicator	Financial performance	Company Value	Capital Structure
DER			1,000
PBV		1,000	
ROA	1,000		

Source: Primary data processed, 2022

After processing the data, all indicators have produced a loading factor that has a value above 0,70. all of which are considered quite good and valid [12].

Discriminant validity

If the correlation value between a construct and its indicators is greater than the correlation between indicators and other constructs, it is decided that latent constructs are able to predict indicators of their block better than with other block indicators [12].

Table 2. Discriminant validity values

Indicator	Financial performance	Company Value	Capital Structure
DER	-0,313	-0,117	1,000
PBV	0,308	1,000	-0,117
ROA	1,000	0,308	-0,313

Source: Primary data processed, 2022

All indicators have met the research model so that they are considered reliable and valid.

3.1.2 Composite reliability and AVE

to produce a good value and be considered reliable, the resulting AVE value must be greater than 0,50 and composite reliability or Cronbach's alpha must be greater than 0,70.

Table 3. Composite reliability and AVE values

Indicator	Cronbach's Alpha	rho_A	Composite Reliability	AVE
Financial performance	1,000	1,000	1,000	1,000
Company Value	1,000	1,000	1,000	1,000
Capital Structure	1,000	1,000	1,000	1,000

Source: Primary data processed, 2022

3.2 Inner model

Table 4. Value of R Square

Variable	R Square	R Square Adjusted
Financial performance	0,098	0,087
Company value	0,095	0,074

Source: Primary data processed, 2022

R-square. R-square is used to evaluate each dependent construct in order to determine the predictive power of the structural model [12]. The resulting R-square value of financial performance only produces a value of 0,098 which means that the model can only explain for variables that can affect financial performance of 9,8% only and the rest will be explained by other variables that are not included in the research domain [12]. Likewise with the value of the company which is only able to explain by 9,5%.

The purpose of Q-square is to see how well the results of the observations relate to the model and its measurement estimates. Q-square can be decided as good if the resulting value is more than 0. The Q-square formula is as follows:

$Q^2 = 1-(1-R_1{}^2)(1-R_2{}^2)\ldots\ldots.(1-R_n{}^2)$

$Q^2 = 1-(1-0{,}098^2)(1-0{,}095^2)$

$Q^2 = 1-(1-0{,}009604)(1-0{,}009025)$

$Q^2 = 1-0{,}98145772$

$Q^2 = 0{,}01854228$

The results of the Q-square calculation (Q^2)that the resulting value is more than 0 so it can be decided that the model used is good enough and can be studied. Then calculate the Goodness of Fit (GoF) value as follows:

GoF formula:
GoF = AVE xR^2
GoF = 1,000 x 0,0965
GoF = 0,0965

Based on the calculation of the GoF value, it produces a value of 0,0965 which indicates that the model used for observations is still lacking because it produces a small value.

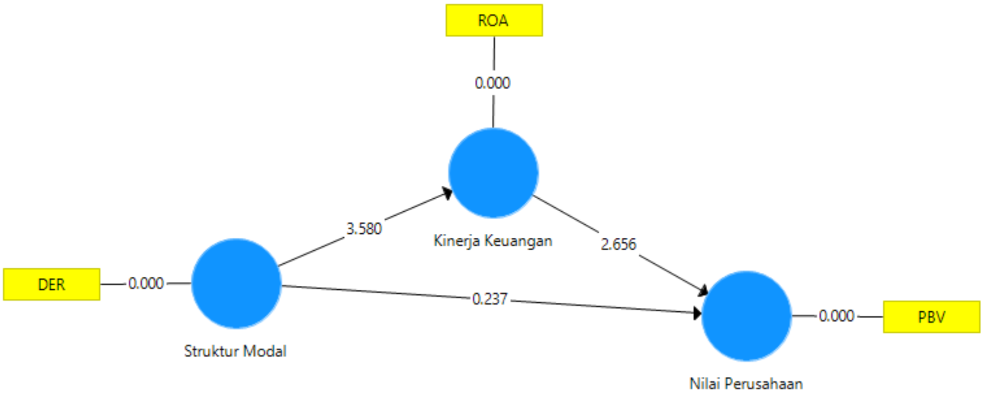

Fig. 1. Structural model

Table 5. Result for inner weight

Correlation	Original Sample	Sample Mean	Standard Deviation	T Statistics	P Values
Financial performance→Company Value	0,301	0.,301	0,119	2,530	0,012
Capital Structure→Financial Performance	-0,313	-0,323	0,089	3,516	0,000
Capital Structure→Company Value	-0,022	-0,014	0,090	0,249	0,804

Source: Primary data processed, 2022

The results of testing the hypothesis are as follows:

a. Capital structure has a positive effect on company value. The resulting t-statistical value of 0,249 is a smaller value than the t-table, which is 1,988 so that the hypothesis is rejected.

Capital structure has no effect on company value because the resulting capital structure is less than optimal. Companies use debt more than capital so investors are afraid when the company defaults. The companies produced in this study have an average DER value above 1 which indicates the company must be more careful in choosing funding sources. In this study, the source of funding taken is not appropriate so that it is not enough to attract investors to increase the value of the company. The capital structure has not been regulated by the management according to its portion so that excessive use of debt is not planned as well as possible so that it does not produce a good capital structure. The results of the study support previous research by Nguyen et al. (2020).

b. Capital structure has a positive effect on financial performance. The resulting t-statistical value of 3,516 is a greater value than the t-table which is only 1,988 so that the hypothesis is accepted.

Capital structure has a positive effect on financial performance. This is because even though the use of debt is more than capital, the company's management is able to utilize the debt properly so as to generate maximum profit. Because in research Van Khanh et al. (2020) said that creditors and shareholders will be afraid if the company fails to manage the company so that the company is required to manage its risks properly. The results of the study support previous research by Mudany et al. (2020) because the company must have thought in advance how the risks in business activities and run in accordance with the company's targets.

c. Financial performance has a positive effect on company value. The resulting t-statistical value of 2,530 is a value greater than the t-table which is only 1,988 so that the hypothesis is accepted.

Financial performance affects the value of the company as financial performance is used as a benchmark by investors to see how healthy the financial condition of a company is. According to Irwanti & Ratnadi (2021) investors will observe the financial performance produced by the company in order to find out the success that has been achieved by a company. The results of the study support previous research by Fadrul et al. (2021).

To explain the indirect effect, that is by using a mediating variable which will be tested using the Sobel test. The results of the indirect effect hypothesis test are as follows:

Table 6. The results of the indirect effect hypothesis test

	SM-KK-NP
Sobel test statistics	2,05345818
One-tailed probability	0,02001408
Two-tailed probability	0,04002816

d. Financial performance is able to mediate capital structure on company value. The resulting t-statistical value of 2,053 is a greater value than the t-table which is only 1,988 so that the hypothesis is accepted.

Based on the results of the hypothesis, the direct effect of capital structure on financial performance and financial performance on company value. Capital structure is used as an indicator for investors to see the highs and lows of a stock. The design related to the company's capital structure is good enough so that the demand for shares is high, which results in good financial performance because investors will flock to put their capital in the company. Yurianda & Masdupi (2019) argues that good financial performance requires strong processes and strategies, one of which is the selection of a good capital structure. The results of the study support previous research by Suzulia et al. (2020) and Yurianda & Masdupi (2019).

4 Conclusion

Based on the inconsistency of previous research, this study examines the gaps that occur by using samples from various industrial sector companies in 2017-2020. The result of this study is that the capital structure cannot affect the value of the company but the capital structure has an effect on financial performance. In addition, financial performance is able to affect company value and financial performance as a mediating variable is able to provide an indirect effect between capital structure on company value. Based on the results of the research, the author provides suggestions, namely for further research to add other indicators so that investors have more considerations so that their investment decisions are right and not misdirected.

References

[1] M. C. Jensen and W. H. Meckling, "Theory of the firm: Managerial behavior, agency costs and ownership structure," *J. financ. econ.*, vol. 3, no. 4, pp. 305–360, 1976, doi: 10.2139/ssrn.94043.

[2] M. C. Jensen and W. H. Meckling, "Theory of the Firm: Managerial Behavior, Agency Cost and Ownership Structure," *J. Financ. Econ.*, vol. 3, pp. 305–360, 1976.

[3] M. Spence, "Job Market Signaling," *Q. J. ofEconomics*, vol. 87, no. 3, pp. 355–374, 1973, doi: 10.1055/s-2004-820924.

[4] V. T. Van Khanh, D. N. Hung, V. T. T. Van, and H. T. Huyen, "A study on the effect of corporate governance and capital structure on firm value in vietnam," *Accounting*, vol. 6, no. 3, pp. 221–230, 2020, doi: 10.5267/j.ac.2020.3.004.

[5] I. Utami, "Pengaruh Struktur Modal Terhadap Nilai Perusahaan (Studi Kasus Terhadap Sub Sektor Perdagangan Eceran Yang Terdaftar di BEI Tahun 2011-2015) Indri," *J. Akuntansi, Audit dan Sist. Inf. Akunt.*, vol. 3, no. 3, pp. 389–397, 2019.

[6] T. T. Nguyen, H. P. Nguyen, N. K. Linh, N. T. Vu, and T. U. Le, "The relationship between capital structure and firm value: Cases of listed companies in the food and beverages industry in Vietnam," *Acad. Account. Financ. Stud. J.*, vol. 24, no. 1, 2020.

[7] D. Yurianda and E. Masdupi, "The Influence of Capital Structure and Intellectual Capital on Firm Value Financial Performance as an Intervening Variable," *Adv. Econ. Res. Bus. Manag.*, vol. 124, 2019.

[8] K. M. Meshack, N. Winnie, K. Okiro, and D. E. Ochieng, "The Effect of Capital Structure on Financial Performance with Firm Size as a Moderating Variable of Non Financial Firms Listed at the Nairobi Securities Exchange," *African Dev. Financ. J. Febr.*, vol. 1, no. 2, pp. 104–121, 2022.

[9] N. P. P. W. Irwanti and N. M. D. Ratnadi, "Good Corporate Governance Moderate the Effect of Financial Performance on Firm Value," *Int. J. Bus. Manag.*, vol. 8, no. 1, pp. 91–101, 2021, doi: 10.24940/theijbm/2021/v9/i3/bm2103-048.

[10] Fadrul, Budiyanto, and N. F. Asyik, "The Effect of Ownership Structure and Corporate Social Responsibility on Financial Performance and Firm Value in Mining Sector Companies in Indonesian," *Int. J. Econ. Dev. Res.*, vol. 2, no. 2, pp. 394–411, 2021.

[11] J. O. Mudany, N. K. Letting, and W. Gituro, "Effects of Capital Structure on Performance : A Critical Review," *J. Financ. Account.*, vol. 4, no. 3, pp. 29–44, 2020.

[12] I. Ghozali and H. Latan, *Partial Least Squares Konsep, Teknik Dan Aplikasi menggunakan Program SmartPLS 3.0 Edisi 2*. Semarang: Universitas Diponegoro, 2015.

[13] M. T. Suzulia, Sudjono, and A. B. Saluy, "The Effect of Capital Structure, Company Growth, and Inflation on Firm Value with Profitability as Intervening Variable (Study on Manufacturing Companies Listed on BEI Period 2014-2018)," *Dinasti Int. J. Econ. Financ. Account.*, vol. 1, no. 2, pp. 95–109, 2020, doi: 10.38035/DIJEFA.