

CHAPTER I

INTRODUCTION

1.1 Background Of The Study

Firm value is a crucial indicator that reflects the performance and attractiveness of an entity in the eyes of investors. In a competitive business context, companies are required to not only focus on increasing profitability, but also to manage capital structure and dividend policy effectively. Various factors can influence a company's value, including profitability, which indicates how effectively a company generates earnings, as well as the capital structure, which reflects the mix of debt and equity financing. In addition, a consistent dividend policy can provide a positive signal to investors and provide confidence in the sustainability of the company cash flow. Understanding the relationship between these factors is important in formulating strategies that attract investors and improve overall company performance.

In Indonesia, several large companies have shown a significant increase in profitability, as evidenced by performance reports showing an increase in net profit and substantial dividend distributions to shareholders. When a company's profitability improves, it grabs the attention of investors, leading to higher stock prices and an increase in the company's overall value. This growth is often backed by a smart approach to managing debt and equity, helping the company reduce costs and use its resources more efficiently. This optimal capital structure plays a role in attracting investors as it shows the financial stability of the company. A consistent

dividend policy also provides a positive signal to the market, where the company is considered a stable and profitable entity, thereby increasing the value of the company.

Although profitability and a good capital structure can contribute to an increase in firm value, not all companies implement a consistent dividend policy. Some companies prefer to retain profits or distribute a limited amount of dividends, citing the need to support business expansion or other investments. This approach may reduce investors' interest in making further investments because they assume that the profits do not immediately provide returns to them. Investors see a consistent dividend policy as an indicator of trust in the company's future cash flow sustainability. Consequently, this decline in investor interest has the potential to reduce the value of the company in the market. In the manufacturing sector, this issue becomes even more important due to the high dependence on investors, as well as fluctuations in company value that can affect long-term operational sustainability.

Firm value is a key measure of a company's performance and its attractiveness to investors, reflecting its ability to generate wealth for shareholders. Several factors can influence a company's value, including profitability, liquidity, capital structure as reflected by leverage, and dividend policy.

In today's competitive market, enhancing firm value involves not just improving profits but also strategically managing financial leverage and governance. Understanding these drivers helps companies develop better strategies for long-term growth and sustainability, aligning management actions with

shareholder interests while optimizing resources for future success. This research explores the main factors influencing firm value, using insights from relevant studies.

Companies with stable profitability and consistent dividend policies generally have higher firm values, as investors see them as stable and profitable entities. Conversely, companies with high debt levels that are not matched by good profitability often experience a decline in value, especially if the company struggles to repay debt or even shows an inability to generate sufficient profits.

Good financial performance, such as consistent revenue and profit growth, is often directly related to an increase in firm value. For example, a company that shows an increase in net income and positive cash flow will usually experience an increase in stock price which will make investors more likely to invest in the company which will ultimately increasing the market value of the company.

Profitability plays a crucial role in affecting a company's value, as it reflects how efficiently a company generates income from its assets or shareholders' equity. Firms with strong profitability are generally more appealing to investors due to the higher potential for returns on their investments. High profitability also allows the company to strengthen its financial position, support business expansion, and provide more stable dividends to shareholders. Companies that demonstrate good financial performance through increased profitability tend to get higher valuations, which are reflected in their stock prices and market capitalization. Because profitability ratios can provide an overview of how investors are related to the

profits they can get, so this ratio is an important consideration for long-term investors when making investment decisions (Wanti & Kumala Sari, 2022).

Previous studies conducted by (Parida et al., 2022) & (Stefanie & Yanti, 2023) found a positive and significant impact of profitability on company value. However, a study by (Yanti et al., 2022) which found that profitability does not influence on firm value.

Capital structure is one of the important factors affecting firm value as decisions regarding funding through debt or equity can impact financial risk and returns for shareholders. Capital structure refers to how a company meets its funding requirements by utilizing a combination of debt and equity. Companies must find efficient and effective ways of funding to meet their funding needs. Efficient and effective funding can only be achieved by companies that have a good capital structure (Marpaung et al., 2022). The selection of the right capital structure is very important because it will affect the company's financial stability, financial risk, and the rate of return for shareholders in order to maximize company value.

Previous studies conducted by (Marpaung et al., 2022) indicate capital structure has a positive but insignificant impact on firm value partially whereas the study conducted by (Diana & Munandar, 2023) which found that capital structure negatively and significantly impacts firm value.

Dividend policy is a moderating variable in this study since the firm's value is determined by its capacity to pay dividends. The decision made by a company on the amount of profit to be distributed to shareholders as dividends and the amount to be retained for reinvestment in the business is known as dividend policy.

Dividend policy can also serve as a signal to investors as a stable dividend rate is considered a good indication of a company's financial prospects (Cordiaz et al., 2021). On the other hand, a company that is highly profitable but does not pay dividends may be seen as less favorable by investors, despite its good financial performance internally.

Earlier research by (Simanjuntak et al., 2019) found that dividend policy enhances the relationship between profitability and firm value. However, this finding contrasts with studies by (Parida et al., 2022) which states that Dividend policy is unable to strengthen the effect of profitability on firm value. Previous studies conducted by (Muhammad Prasetya et al., 2023) & (Yuswandani et al., 2023) which suggests that dividend policy does not have a moderating effect on the correlation between capital structure and firm value..

Earlier research by (Itra et al., 2023), (Parida et al., 2022) & (Stefanie & Yanti, 2023) indicates that profitability has a significant influence on firm value. Then, the research conducted by (Nopianti & Suparno, 2021) & (Anggraini & MY, 2021) highlighted the positive impact of capital structure on company value. Then, research on dividend policy as a moderating variable conducted by (Sintyana & Artini, 2019) found that dividend policy positively affects firm value. The difference between previous research and current research is the difference in moderating variables, which uses dividend policy. in this study, using the research year period from 2017-2023.

According to the explanation provided above, the title of this study is **“The Effect of Profitability and Capital Structure On Company Value with Dividend**

Policy as Moderating Variable.” The aim of this research is to provide new insights into how profitability and capital structure interact with dividend policy in influencing firm value. By identifying the relationship between these variables, this research will contribute to a better understanding of the dynamics that influence firm value, especially in the context of companies operating in Indonesia.

It is expected that this research will not only enrich the literature in the field of financial management, but also provide practical guidance for investors and company managers in formulating strategies that can increase firm value. Thus, the findings of this research are expected to be a useful reference for academics and practitioners to develop more effective policies in managing profitability, capital structure, and dividend policy, so as to attract investor interest and support sustainable company growth.

1.2 Problem Limitation

In order to make this research to be more focused and does not expand from the discussion in question, the researcher limits it to the scope of the research including:

1. The sample for this study consists of manufacturing companies listed on Indonesia Stock Exchange based on S&P Capital IQ in the 2017-2023 period.
2. This research is confined to analyzing the independent variables of profitability and capital structure, along with the dependent variable of firm value.

3. The research only focuses on dividend policy as a moderating variable on the impact of profitability and capital structure on firm value.

1.3 Problem Formulation

Based on the background of the study presented by the researcher above, the researcher formulates the problems in this study with the following details:

1. Does Profitability have a significant effect on firm value?
2. Does Capital Structure have a significant effect on firm value?
3. Does Dividend Policy moderate the relationship between Profitability on Firm Value?
4. Does Dividend Policy moderate the relationship between Capital Structure on Firm Value?

1.4 Objective of the Research

Based on the research problem above, the objectives of this research are:

1. To provide empirical evidence regarding the effect of profitability on firm value.
2. To provide empirical evidence on the effect of capital structure on firm value.
3. To provide empirical evidence regarding the role of dividend policy in the relationship between profitability on firm value.
4. To provide empirical evidence regarding the role of dividend policy in the relationship between capital structure on firm value.

1.5 Benefit of the Research

1. For academics

This research can serve as a reference for future researchers who want to develop or deepen the study of the influence of financial factors on firm value. This study provides an empirical basis regarding the role of dividend policy as a moderating variable, so future researchers can explore other variables or use different analytical methods to examine the relevance and strength of this relationship in various industrial sectors.

2. For practitioners

For practitioners, especially financial managers and investors, the results of this study provide clearer insights into how profitability and capital structure affect firm value. An understanding of dividend policy as a moderating factor can help practitioners make more informed decisions in determining the optimal dividend strategy and capital structure, so as to increase firm value and attract more investors.