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The Effect of Debt Equity Ratio, Dividend Payout Ratio, and Profitability on the Firm Value

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Abstract: The purpose of this study is to explain and analyze the influence of Debt Equity Ratio (DER), Dividend Payout Ratio (DPR), profitability to the value of manufacturing companies on the Indonesia Stock Exchange. The population in this study are manufacturing companies that are listed and are still active on the Indonesia Stock Exchange (BEI) from 2016 to 2018, amounting to 138 companies. Sampling was done by purposive sampling method. Of these, there are 15 sample companies for 3 years that meet the established research sample criteria. The results of the study explain that Debt Equity Ratio (DER) has a positive and significant effect on firm value. Dividend Payout Ratio has a positive and significant effect on firm value. Dividend policy determines how much profit a shareholder will get. Profitability has a positive and significant effect on firm value, this shows that the higher the profitability (profitability), the higher the value of the company.

Keywords: Debt Equity Ratio, Dividend Payout Ratio, profitability, Firm Value

I. INTRODUCTION

The number of companies in the industry, as well as the current economic conditions, have created intense competition among manufacturing companies. Competition in the manufacturing industry makes each company improve its performance so that its goals can still be achieved. The main objective of the company is to increase the value of the company by increasing the prosperity of the owner or shareholders. In accordance with the statement that the main purpose of companies that have gone public is to increase the prosperity of owners or shareholders in order to influence the value of the company (Salvatore, 2005). The welfare of shareholders, shown through the market price per share of the company, which is also a reflection of investment decisions, funding, and asset management because, basically a business decision is valued based on the impact it has on stock prices (Moeljadi, 2006: 25).

Firm value is very important because high company value will be followed by high shareholder prosperity (Brigham, 1996). The higher the stock price, the higher the company's value. Managers are required to make decisions that consider all stakeholders in maximizing the value of the company in the long run because, managers will be assessed performance based on the success of achieving goals (Jones, 2007).

Firm value can be seen from the Price Book Value (PBV) which is a comparison between the stock price and the book value per share (Brigham & Houston, 2006). Good companies generally have a PBV ratio of one (> 1), which indicates that the market value of shares is greater than the book value of the company. The higher the PBV ratio the higher the valuation of the investor compared to the funds invested in the company so that the greater the opportunity for investors to buy shares of the company (Brigham & Houston, 2006).

Investors often value a company by looking at the value of the company's shares. Appraisal of the value of company shares there are three important types of valuation. The assessment is an assessment of book value (market value), market value (market value) and intrinsic value (intrinsic value) (Jogiyanto, 2010: 88). One approach in determining the intrinsic value of a stock is Price to Book Value (PBV). PBV or price-to-book value ratio is the relationship between the stock market price and book value per share.

At present, the business world is very dependent on funding issues. The funding decision is related to the company's decision to find funds to finance investment and determine the composition of funding sources derived from retained earnings, debt, and equity in financing investments and the company's operational activities that will have an impact on the company's value. Capital structure refers to the different choices that companies use to finance their capital (Saleem et al. 2013). Capital structure decisions are decisions in choosing debt and equity funding (Brealey &

Myers, 2006: 7). The optimal capital structure must reach a balance between risk and return so as to maximize stock prices. (Brigham & Houston, 2006: 7).

The debt policy explains that corporate finance (financial policy) can be used to optimize the value of the firm. According to trade-off theory, managers can choose a debt ratio to maximize the value of the company. The value of the company will be reflected in the share price. Maximizing the value of the company is not only the value of equity that must be considered but the type of all financial sources such as debt, warrants or preferred stock. Optimizing company value which is the company's goal can be achieved through the financial management function, where one financial decision is taken will affect other financial decisions and have an impact on the company's value (Brigham & Houston, 2006).

Dividend policy is one important aspect of the goal of maximizing the value of the company. Management has two alternative treatments for net income after tax or Earnings After Tax (EAT), which is to share it to shareholders in the form of dividends, or reinvested into the company as retained earnings. Typically, part of the EAT is divided into dividends and some are reinvested. Therefore, management must make a policy about the amount of EAT distributed as dividends. If the company decides to divide the profits derived as dividends, it will reduce the amount of retained earnings which ultimately reduces the source of internal funds used to develop the company. Companies can reduce agency costs by distributing dividends, this is because it reduces the amount of company cash flow that is often used by managers to be used wastefully (inefficiently).

Company value can be seen from the company's ability to pay dividends. The amount of dividend that is shared can affect the stock price. If the dividend paid is high then the stock price tends to be high so the value of the company is also high. However, if the dividends paid to shareholders are small then the company's share price is also low. Thus, a large dividend will increase the value of the company (Harjito and Martono, 2010: 115).

Dividend payments are part of company monitoring. Companies tend to pay greater dividends if insiders have a lower proportion of shares. Dividend payments to shareholders will reduce the sources of funds controlled by managers, thereby reducing the manager's power and making dividend payments similar to monitoring the capital market that occurs if the company obtains new capital (Harjito, 2010).

Bird in the Hand Theory argues that there is a relationship between company value and dividend policy, where the value of the company will be maximized by a high dividend payout ratio because investors assume that the risk of dividends is not as high as the risk of capital increase. Investors prefer profits in the form of dividends than profits expected from an increase in the value of capital.

One important indicator for investors in assessing the company's prospects in the future is to see the extent of the company's profitability growth (Sartono, 2008). High profitability reflects the company's ability to generate high profits for shareholders. The greater the profits obtained, the greater the company's ability to pay dividends, and this has an impact on increasing the value of the company. With a high profitability ratio owned by a company will attract investors to invest their capital in the company.

This research is expected to be one of the empirical study materials regarding debt policy, dividend policy, profitability and company value. In addition, it is expected to be a reference in determining debt strategy and policy, dividend policy, and profitability to be able to increase the value of the company in manufacturing companies listed on the Indonesia Stock Exchange (IDX).

II. LITERATUR REVIEW

Firm Value

Jones (2007) the value of the company is the market value of the debt securities and corporate equity in circulation. Company value is an investor's perception of the company's success rate which is often associated with stock prices (Sujoko and Soebiantoro, 2007). High stock prices make the value of the company is also high. The existence of PBV is very important for investors to determine investment strategies in the capital market because through price book value, investors can predict stocks that are overvalued or undervalued (Riyanto, 2010: 49).

Debt Equity Ratio

Schoedar (2001) in Mamduh (2007: 61) "Financing activities result from obtaining resources from owners, providing owners with a return of a return on their investment, borrowing money and repaying the amount borrowed, and obtaining and paying for other resources from a longterm creditor. Funding policy within a company must aim for mutual prosperity. Funding decisions consider and analyze sources of funds that are economical for the company to finance its routine and investment needs.

Dividend Payout Ratio

Dividend policy determines the distribution of profits between payments to shareholders and corporate reinvestment. Retained earnings are one of the most important sources of funds to finance company growth, while cash dividends are cash flow set aside for shareholders (Weston, 2010). Dividend policy is a decision about whether to share profits or hold it back to be reinvested in a company (Brigham & Houston, 2006).

Profitability

Profitability illustrates the ability of a business entity to generate profits using all its capital. This is in accordance with the statement of Weston (2006) "Profitability measures management objectiveness as indicated by return on sales, assets and owners equity." According to Riyanto (2010), the way to assess the profitability of a company is diverse and depends on earnings and which assets or capital will be compared with one another.

III. DATA, VARIABLES, AND METHODOLOGY

3.1. Types of research

This study uses a pattern of explanation (level of explanation). Explanation research is research that aims to describe the effect between two or more variables. Based on data from companies listed on the Indonesia Stock Exchange, it is known that the companies listed in 2016-2018 totaled 138 manufacturing companies. Of these, there are 15 sample companies for 3 years that meet the research sample criteria

3.2. Variable

a. Dependent Variable

Debt Equity Ratio (DER)

debt policy owned by the company, it can show the risk of uncollectible debt.

$$\textit{Debt to equity ratio} = \frac{TotalDebt}{TotalEquity}$$

Dividend Payout Ratio (DPR)

Dividend policy determines the distribution of profits between payments to shareholders and corporate reinvestment

$$\textit{Dividend Payout Ratio} = \frac{devidend\ per\ share}{earning\ per\ share}$$

Profitability

the overall level of company operating efficiency.

$$\text{Return On Asset} = \frac{net\ \mathrm{Pr}\,ofit}{Total\ Asset}$$

b. Independent Variable

Company Value

Company value is an investor's perception of the company's success rate that is often associated with stock prices

$$\text{PBV=} \quad \frac{\mathrm{Pr}\,ice\ per\ share}{Book\,Value\ per\ share}$$

3.3. Research Method

Research Conceptual Framework

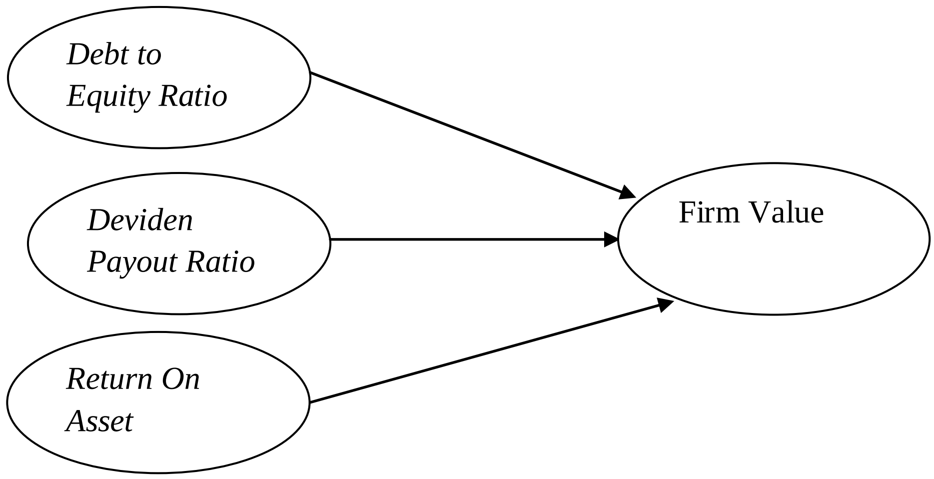

Figure 1. Research Conceptual Framework

Data analysis method

The method used to determine the effect of debt policy, dividend policy, company size and managerial stock ownership on firm value is used multiple regression analysis (Gujarati, 2000). Calculation of multiple linear regression analysis was carried out with the help of Statistical Package for Social Science (SPSS) 15.0 for windows.

$Y = a + b_1X_1 + b_2X_2 + b_3X_3 + e$

IV. RESEARCH RESULTS

The multiple regression analysis methods are used to see whether there is an influence of the Dividend Payout Ratio (DPR) variable and profitability on company value.

Table 1. Results of Benrganda Linear Regression Analysis

Research variable	B	t	sig.	
Constanta	-0.198			
Debt Equity Ratio	0.413	3,749	0,001	Significant
Deviden Payout Ratio	0.542	4,934	0,000	Significant
Profitabilitas	0.0249	2,166	0,036	Significant

The Effect of Debt to Equity Ratio on Firm Value

The value of t arithmetic for the variable Debt Equity Ratio (DER) is 3.749 with a significance of 0.001 smaller than statistically significant at α = 5% so it rejects H0 which means that Debt Equity Ratio (DER) has a positive and significant effect on the value of the company, this It means that the recall of debt policy will also be followed by an increase in the value of the company.

Effect of Dividend Payout Ratio on Firm Value

The value of t arithmetic for the variable Payout Ratio (DPR) is 4.934 with a significance of 0,000 smaller than statistically significant at α = 5%, thus rejecting H0 which means that Dividend Payout Ratio (DPR) has a positive and significant effect on firm value, this means that an increase in dividend policy will also be followed by increased corporate value.

The Effect of Return On Assets on Firm Value

The value of t arithmetic for the profitability variable is 2.166 with a significance of 0.036 smaller than the statistical significance at α = 5%, thus rejecting H0 which means that profitability has a positive and significant effect on firm value, this means that an increase in profitability will be followed by an increase in company value.

V. DISCUSSION

Based on the results of inferential statistical analysis, there is evidence that debt policy has a positive and significant effect on firm value. Determination of optimal debt policy targets is one of the main tasks of company management. Debt policy (Debt Equity Ratio) is the proportion of funding with debt (debt financing) companies, namely the ratio of leverage (leverage) of the company, thus, debt is an element of the company's debt policy. Debt policy is the key to improving company productivity and performance. Debt policy theory explains that the company's financial policy in determining debt policy (a mix of debt and equity) aims to optimize the value of the firm.

The results of this study found that there was a positive and significant effect on firm value. This result can be explained that the use of debt in debt policy can control excessive use of free cash flow so that management is not involved in unprofitable investment projects. Payment of debt installments and other financial expenses can reduce the agency's problem of using free cash flow. The use of debt will bring additional oversight from the creditor so that management works for the benefit of the company. This condition will be responded positively by shareholders which are reflected in an increase in share prices.

These findings are supported by trade-off theory, where according to trade-off theory, managers can choose the debt ratio to maximize the value of the company. The trade-off model assumes that the company's debt policy is the result of trade-offs from tax profits using debt at a cost that will arise as a result of using that debt. The essence of trade-off theory in debt policy is to balance the benefits and sacrifices that arise as a result of using debt. As far as the benefits are greater, additional debt is still permitted.

Based on the results of inferential statistical analysis, there is evidence that dividend policy has a positive and significant effect on firm value. The dividend policy (Dividend Payout Ratio) determines how much profit a shareholder will get. The profits to be gained by these shareholders will determine the welfare of the shareholders which is the company's main goal. The greater the dividends distributed to shareholders, the performance of the issuer or company will be considered better as well and ultimately a company that has good managerial performance is considered profitable and of course, the assessment of the company will be better too, which is usually reflected through the level of the company's stock price .

If the company increases dividend payments, it might be interpreted by investors as a signal of management's expectation about the company's improved performance in the future, so that dividend policy has an influence on the company's value.

Based on the results of statistical analysis in this study, it was found that profitability had a significant positive effect on firm value, this indicates that the higher the profitability, the higher the firm's value. The higher the company's ability to generate profits, will increase the value of the company as indicated by an increase in the company's stock price Paranita, 2007, Nurhasanah, 2012). Companies that have large profitability every year tend to be in demand by many investors. Investors assume that companies that have large profits will also produce large returns. This is captured by investors as a positive signal from the company so that it will increase investor confidence and will facilitate company management to attract capital the form of shares.

The higher profitability of the company will also increase earnings per share (EPS or earnings per share) of the company (Machfoedz, 2009). An increase in EPS will make investors interested in investing their capital by buying company shares. This condition causes a positive relationship between profitability and stock prices where the high share price will affect the value of the company.

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VI. CONCLUSION

This study examines the effect of Debt to Equity Ratio, Dividend Payout Ratio, profitability on firm value. Debt Equity Ratio (DER) has a positive and significant effect on firm value. This result can be explained that the use of debt in the capital structure can control excessive use of free cash flow so that management is not involved in unprofitable investment projects. Dividend Payout Ratio has a positive and significant effect on firm value. Dividend policy determines how much profit a shareholder will get. Profitability has a positive and significant effect on firm value, this shows that the higher the profitability (profitability), the higher the value of the company. Implications for the company to continue to increase the value of the company, the company is expected to be able to maintain optimal capital structure conditions through the use of debt. In addition, so that the public continues to believe in the company's prospects, the company is expected to know what criteria are the basis for investors to invest their capital. For investors and potential investors of companies listed on the Indonesia Stock Exchange to be more careful and also pay attention to aspects of managerial stock ownership as a consideration in investing

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