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Research Paper

Effect of Good Corporate Governance, Financial Leverage and Firm Size on Firm Value with Profitability as an Intervening Variable

(Case Study of Banking Companies Included in the ASEAN Corporate Governance Score Card Country Reports and Assessments)

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ABSTRACT

The purpose of establishing a company in the context of financial management consists of short-term goals, namely achieving maximum profit using existing resources and long-term goals to increase company value. The company's value is used as an indicator of the success of the company's management in managing its current and future business so as to create confidence for investors to invest their capital. The purpose of this study was to determine the effect of good corporate governance, financial leverage, and firm size on firm value with profitability as an intervening variable. The study population consisted of 22 banking companies included in the ASEAN corporate governance score card country reports and assessments with 88 research samples from 2016 to 2019. This type of quantitative descriptive research used path analysis techniques. Based on the results of the analysis conducted, it is found that good corporate governance and firm size have a positive and insignificant effect on profitability; financial leverage has a positive and significant effect on profitability. Good corporate governance and profitability have a positive and insignificant effect on firm value, financial leverage and firm size have a positive and significant effect on firm value. Profitability is able to mediate good corporate governance, financial leverage, and firm size on firm value, but it is not significant.

Keywords: Good Corporate Governance, Financial Leverage, Firm Size, Firm Value, Profitability

INTRODUCTION

Increasingly tighter competition in the world of business and the economy in the current era of globalization have encouraged business actors to continue to strive to improve their company performance. On the other hand, the existence of a global market requires companies to be able to show their best performance both in regional and international markets. This means adding to the long list of company competitors to get investors to finance the company's operations. Competition in the world of business and economy causes the company's performance aspect to be very important with the aim of building and ensuring the life of the company.

The goal of profit maximization is often associated with financial factors. Financial factors relate to financial management or financial management, starting from how a company looks for sources of funds, obtains sources of funds, and allocates these sources of funds in order to be effective and efficient in their use.

Harjito and Martono (2010) summarize that financial management consists of the function of financial factors which are included in investment decisions, funding (including dividend policy) and asset management decisions.

The purpose of establishing a company in the context of financial management consists of short-term goals, namely achieving maximum profit using existing resources and long-term goals to increase company value. The company's value is used as an indicator of the success of the company's management in managing its current and future business so as to create confidence for investors to invest their capital.

According to Husnan and Pudjiastuti (2012), company value is the price a prospective buyer is willing to pay if the company is sold. Harmono (2018) states that company value is the company's performance as reflected by the share price formed by the demand and supply of the capital market which reflects the public's assessment of the company's performance. Sartono (2010) suggests that company value is the selling value of the company as an operating business. The value of a company is very important because it can reflect the company's performance and the prosperity of shareholders who have invested in a company.

Every company is required to increase its corporate value, because company value is a factor that investors need to consider to invest. Increasing the value of a company is a long-term goal that is reflected in the market price of its shares. The share price indicator is used to reflect the value of the company because the stock price is the price a potential buyer is willing to pay if an investor wants to have proof of ownership of a company.

The Indonesia Stock Exchange through the Composite Stock Price Index (IHSG) is an indicator that reflects the trend of stock price movements in Indonesia (Suharti and Mariah, 2011). Currently, the phenomenon of the movement of the ISHG index performance compared to the indexes of several other countries in Southeast Asia in 2019 is in the fourth position. Even though in 2018 ISHG was in second place after the Philippines. This means that there is a tendency for the decline in stock market value which is quite high in many companies in Indonesia compared to other countries in Southeast Asia. For more details, the following shows the value and percentage of stock index movements in several Southeast Asian countries.

One of the non-financial instruments that is an indicator of company value in this study is good corporate governance (GCG). GCG is a system that regulates and controls the company to create value added for all shareholders (stakeholders).

GCG practices can increase company value, improve financial performance, reduce the risk that the board may take with decisions that benefit itself, and generally increase investor confidence. On the other hand, bad GCG practices can reduce the level of investor confidence (Newell and Wilson, 2002).

In Indonesia, GCG is still classified as weak in the quality of its implementation. The phenomenon that occurs in most companies in Indonesia is that they have not been able to carry out professional company management. Other studies also show that the level of investor protection in Indonesia is the lowest in Southeast Asia.

In corporate finance theory, debt finance and equity finance are the main sources of external finance. But the problem is how they should be structured to minimize agency costs and maximize firm value. The concept of leverage is very important for demonstrating financial analysis considering the trade off between the risk and benefit ratios of the best decision to use debt from various angles. It is the financial manager's job to plan, analyze, and control activities. Companies that have a high level of financial leverage can cause financial distress to be able to settle their debt obligations. This is in line with the statement (Torok and Cordon, 2002), the greater the proportion of debt to equity, the greater the overall business risk. Indeed, in principle, high debt can reduce tax expenditures, thereby increasing corporate value. However, debt that is too high also makes the company's financial condition unhealthy so that it can reduce the company's value. Therefore, the size of the use of debt can affect the value of the company. So leverage is a ratio that measures how much the company uses financial leverage (Brigham and Houston, 2017).

Apart from GCG and leverage, another variable that has also been identified as having an impact on firm value is company size or often known as firm size.

Brigham and Houston (2017) explain that company size is the size of a company that is shown or valued by total assets, total sales, total profits, tax expenses and others. company size can be interpreted as the size of the company seen from the amount of equity value, company value, or the results of the total asset value of a company.

Firm value can also be influenced by the size of the profitability generated by the company. Profitability is the company's ability to earn profits in relation to sales, assets or total assets and own capital. The level of profitability is used as a reference for capital owners in determining whether or not to invest in the company. If the level of profitability in a company continues to increase, investors will tend to choose to invest in that company. As stated by Aulia and Moeljadi (2016), it is explained that companies that can increase their profit stably, then this is seen as a positive signal by investors regarding company performance.

The purpose of this study was to determine the effect of good corporate governance, financial leverage, and firm size on firm value with profitability as an intervening variable.

RESEARCH METHODS

Based on the type of data used, this research is a type of quantitative research, namely research in which the data is obtained and analyzed in the form of numbers, starting from data collection, interpretation of the data and the appearance of the results so that the data analysis uses quantitative analysis (inference). According to Sugiyono (2016), what is meant by quantitative data analysis is data analysis using statistics. The statistics used can be in the form of descriptive and inferential/inductive statistics. Inferential statistics can be in the form of parametric statistics and non-parametric statistics. The data from the analysis results are then presented and discussed. Data presentation can be in the form of tables, frequency distribution tables, line charts, bar charts, pie charts and pictograms. The discussion of the research results is an in-depth explanation and interpretation of the data that has been presented.

The study population consisted of 22 banking companies included in the ASEAN corporate governance score card country reports and assessments with 88 research samples from 2016 to 2019.

This type of quantitative descriptive research used path analysis techniques.

RESULT

Overview of the ASEAN Corporate Governance Score Card

The ASEAN corporate governance (CG) scorecard is a standard for implementing GCG practices based on the principles of the Organization for Economic Cooperation and Development (OECD) Corporate Governance issued by the ASEAN Capital Market Forum.

ACGS originated from the initiative of the Association of Southeast Asian Nations (ASEAN) through the ASEAN Capital Markets Forum (ACMF) in terms of regional capital market integration in the ASEAN capital market. ACGS provides a methodology and benchmarks in terms of the principles of developing corporate governance in Southeast Asia. The methodology and benchmarks are expected to provide comparative information for foreign investors and external capital managers to be part of the investment decision-making process.

This initiative was carried out in conjunction with efforts to achieve convergence in ASEAN as an economic community by 2015. Broadly speaking, the implementation plan is expected to achieve the goals of the ASEAN Economic Community.

The ASEAN CGS aims to raise the standards of overall corporate governance of companies publicly listed with the Association of Southeast Asian Nations, as well as increase their visibility to investors, fostering the unwavering commitment and wholehearted efforts of Southeast Asian countries to encourage their respective regions to become beacons of international standard corporate governance and to promote ASEAN as a wise investment destination.

The Asian Development Bank (ADB) in partnership with the ASEAN Capital Markets Forum (ACMF) has jointly developed a corporate governance assessment methodology in ASEAN using a scorecard system based on best practice with international standards.

The ASEAN CG Scorecard assessment is carried out based on principles that include:

1. Shareholders' rights
2. Equal treatment among shareholders
3. The role of shareholders
4. Information disclosure and transparency
5. Responsibilities of the board of directors/commissioners.

The ASEAN CGS evaluation was carried out by ACMF to the Domestic Ranking Bodies (DRB) in each ASEAN participating country, followed by a peer review conducted by DRB for neighboring countries participating in the region.

Hypothesis Testing

Based on the data processing that has been done, the results can be used to answer the hypothesis in this study. Hypothesis testing in this study was carried out by looking at the t-statistics and p-values. The research hypothesis can be stated as accepted if the p-values<0.10. The following are the results of hypothesis testing obtained in this study through the inner model:

Table 1. T-Statistics and P-Values

Hypothesis	Effect	$T_{statistik}$	P_{Value}	Result
H_1	Good Corporate Governance » Profitability	0.212	0.823	Rejected
H_2	Financial Leverage » Profitability	2.623	0.009	Accepted
H_3	Firm Size » Profitability	0.277	0.782	Rejected
H_4	Good Corporate Governance » Firm Value	0.500	0.617	Rejected
H_5	Financial Leverage » Firm Value	2.091	0.037	Accepted
H_6	Firm Size » Firm Value	1.754	0.080	Accepted
H_7	Profitability » Firm Value	1.277	0.202	Rejected
H_8	Good Corporate Governance » Profitability » Firm Value	0.170	0.865	Rejected
H_9	Financial Leverage » Profitability » Firm Value	0.224	0.823	Rejected
H_{10}	Firm Size » Profitability » Firm Value	1.057	0.291	Rejected

Based on the results of the analysis conducted, it is found that good corporate governance and firm size have a positive and insignificant effect on profitability, financial leverage has a positive and significant effect on profitability.

Based on the results, good corporate governance and profitability have a positive and insignificant effect on firm value, financial leverage and firm size have a positive and significant effect on firm value.

Profitability is able to mediate good corporate governance, financial leverage, and firm size on firm value, but it is not significant.

CONCLUSION AND SUGGESTION

Conclusion

Based on the results of the analysis conducted, it is found that good corporate governance and firm size have a positive and insignificant effect on profitability, financial leverage has a positive and significant effect on profitability. Good corporate governance and profitability have a positive and insignificant effect on firm value, financial leverage and firm size have a positive and significant effect on firm value. Profitability is able to mediate good corporate governance, financial leverage, and firm size on firm value, but it is not significant.

Suggestion

Some suggestions that can be used as a follow-up are as follows:

1. For the Company

a. There are many factors that have an impact on firm value, including good corporate governance, financial leverage, firm size and profitability. For the company to maintain the maximum value of each of these variables because it is proven to have a positive effect on firm value.

b. So that each of the sample companies continues to increase the value of its company both from financial and non-financial elements so that it is able to compete in regional and even international markets so as to provide a positive image for investors to invest.

2. For investors and potential corporate investors

a. It is expected to pay attention to any factors that affect firm value, especially the level of use of corporate debt or financial leverage as a basis for making investment decisions in the capital market.

b. Always pay attention to the movement of the stock price index as a reference or consideration for making investment decisions.

c. In addition to the factors that have been analyzed in this study, in providing an assessment of a company, investors should also pay attention to other factors that can affect the value of a company.

3. For Further Researchers

a. This research is limited to examining the variables of good corporate governance, financial leverage, firm size, firm value and profitability. It is recommended that further researchers add other variables that have not been included in this study in order to expand this research.

b. Further researchers can also increase the sample and scope of the research in order to generalize the research results.

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