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Review article

How Does Company Performance, Systematic Risk and Capital Structure Affect the Corporate Value: Empirical Study on the IndonesianCapital Market

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Abstract *- A. Background: Increasing corporate value is the main goal of managers to maximize shareholder wealth. Three interrelated factors determine corporate value, namely company performance, systematic risk, and capital structure. Systematic risk is the main factor that directly affects the corporate value or indirectly through company performance and capital structure. At the same time, company performance is the second factor that influences corporate value directly or indirectly through capital structure.*

B. Methods: *The sample used is 33 companies that are consistently listed on the LQ45 index from 2014 to 2019, considering that these companies are the most liquid securities companies and their trading volume is relatively large so that they can reflect the actual condition of the Indonesian Capital Market. The data used are 165 observation panel data.*

C. Results: *Partially, Systematic Risk and Capital Structure have a significant negative effect on Corporate Value, while Company Performance has a significant positive effect on corporate Value. Systematic Risk and Company Performance partially have a significant negative effect on Capital Structure.*

D. Conclusion: *Company Performance is the most dominant factor affecting Corporate Value, while Capital Structure is the weakest factor affecting Corporate Value. Compared with Company Performance, Systematic Risk is the more dominant factor affecting Capital Structure.*

Keywords *- Company Performance, Systematic Risk, Capital Structure, Corporate Value.*

I. INTRODUCTION

Increasing corporate value is the main goal for every manager to maximize shareholder wealth. Therefore, managers always try to make policies that can encourage corporate value improvement. One of the common policies undertaken by managers to increase corporate value is to determine the optimal capital structure. The company is expected to have sufficient funds for investment development with minimal capital costs to increase corporate value with an optimal capital structure. Several studies have proven that capital structure has a significant negative effect on corporate value[1], [2], while other studies have shown that capital structure has a positive effect on corporate value[3], [4], [5], but on the other hand some studies prove that capital structure does not significantly affect corporate value[6].

In general, companies use different capital structures, each of which has its own financial decisions. The optimal capital structure decision is a difficult task for managers; on the one hand, risks and costs must be minimized; on the other hand, it must provide more profits and must also be able to increase shareholder wealth. One of the main keys to the optimal capital structure is company performance. Companies that have limited funding from internal sources can seek funding from debt. The use of debt not only incurs capital costs but can also provide tax-saving benefits[7]. Tradeoff Theory[8]states that companies always consider costs and benefits in determining how much debt and equity will be used as capital. If the company is very profitable, then the company will prefer financing with debt to increase corporate value because a capital structure that uses more debt will provide more tax-saving benefits. Several studies have proven that company performance is positively related to capital structure[9], [10], [11]. The higher the company's performance, the greater the use of debt, hoping that the greater the tax savings obtained. But, if a company has low performance, then debt is more likely to encourage greater bankruptcy.

However, according to the Pecking Order Theory, if the company has high performance, then internal financing will be used to finance new projects that can increase the corporate value[12]. Several studies have shown that company performance is negatively related to capital structure[13], [14]. A capital structure whose proportion is more debt than equity will cause a high interest expense, impacting the company's profitability. Therefore,

companies that have high profitability tend to choose to use a capital structure whose proportion is more sourced from equity to finance new projects that can increase the corporate value[15], [16], [17]. Using a capital structure that is more sourced from equity is intended not to cause a higher interest expense because the higher interest expense can reduce company performance and value[18].

With these contradictions, this study tries to find empirical evidence of the influence of company performance on capital structure in Indonesia. This study only limits the company's performance which is emphasized on the aspect of financial performance which is proxied by ROA, because ROA shows better performance measurements[19], and ROA represents the interests of shareholders more. This study is intended to examine the systematic role of risk and company performance in mediating the effect of capital structure on corporate value. The concept of influence between variables in this study is a tiered effect by placing unsystematic risk and company performance as intervening variables.

A. Hypothesis Development

a) The Influence of Company Performance on Corporate Value

Company performance determines corporate value. Companies with high company performance will have the ability to distribute dividends to their shareholders. For investors in the capital market, companies that are consistently able to distribute dividends have their charm so that many potential investors are interested in buying their shares. The increasing demand for shares has pushed up the price of these shares, which can increase corporate value. Several studies have proven that company performance can directly improve corporate value[20], [21].

H1: Company performance has a significant positive effect on corporate value.

b) Effect of Systematic Risk on Corporate Value

Harry Markowitz (1952) has stated that investors face two risk groups, namely Systematic risk and unsystematic risk[22]. Unsystematic risk is a risk that comes from the company's internal conditions so that it is controllable. Unsystematic risk can be reduced, even eliminated, if a good diversification of investments is made by forming a portfolio[23]so that unsystematic risk does not cause problems. Conversely, systematic risk originates from the company's external factors, so it is uncontrollable. Systematic risk originates from the economic conditions in which the company operates. This economic condition affects all companies, so that it cannot be eliminated using diversification. Companies have different sensitivity to economic conditions. Companies that have a high sensitivity to external conditions will have a high systematic risk. The higher the systematic risk of a company, the less attractive it is to potential investors, thereby impacting the decline in corporate value.

H2: Systematic risk has a significant negative effect on corporate value. The higher the systematic risk, the lower the corporate value.

c) The Effect of Capital Structure on Corporate Value

The use of a capital structure in which the proportion of more debt than equity will cause a greater share of profits paid to creditors in the form of interest so that net income entitled to shareholders will be less. As net income decreases, dividends paid out to shareholders are also getting smaller. In the end, the decline in dividends becomes negative information for potential investors, causing a decline in share prices. A Decline in stock prices causes a decrease in corporate value. So, more use of debt than equity in capital structure will cause a decrease in corporate value.

H3: Capital structure has a significant negative effect on corporate value. The greater the use of debt, the smaller the corporate value.

d) Effect of Company Performance on Capital Structure

An Optimal capital structure is one of the objectives of the company's financial policy. With an optimal capital structure, the company will have sufficient funds to fund development investments with minimal capital costs to increase the value. Capital structure is very dependent on company performance. According to the Pecking Order Theory, companies with high performance tend to use financing sourced from equity to finance new projects that can increase corporate value[12]. Several studies have proven that the performance of companies is negatively related to capital structure[13], [14], meaning that companies that have high performance tend to use more funding sources from equity than sources of funds from debt.

H4: Company performance has a significant negative effect on capital structure. The higher the company's performance, the smaller the funding sourced from debt.

e) Effect of Systematic Risk on Capital Structure

Harry Markowitz (1952) has stated that investors face two risk groups, namely Systematic risk and unsystematic risk[22]. Systematic risk is the risk that comes from external factors, so that it is uncontrollable. This external condition affects all companies, so that it cannot be eliminated using diversification. Each company has a different sensitivity to external conditions. Companies that have a high sensitivity to external conditions will have a high systematic risk. The higher the systematic risk, encouraging companies to be more careful. Therefore companies with high systematic risk must reduce their debt[24]. The higher the systematic risk, the company tends to use more equity than the debt in its capital structure. The use of greater equity is intended to avoid the failure of interest payments. Failure to pay interest is categorized as a failure that can lead to bankruptcy demands by creditors.

H5: Systematic risk has a significant negative effect on capital structure. The higher the systematic risk, the smaller the funding from debt.

f) Effect of Systematic Risk on Company Performance

The risk is divided into two, namely systematic risk and unsystematic risk[22]. Systematic risk is the risk that comes from external factors, especially from economic conditions. Therefore, systematic risk is also referred to as market risk. Because it is sourced from the company's external factors, the company can avoid systematic risk so that it always exists. Therefore investors in the capital market cannot avoid or reduce systematic risk by diversifying investment portfolios.

Companies that operate in an environment with uncertain market conditions will face serious problems. The company's sales are difficult to predict precisely. As a result, the company cannot predict the profit that will be obtained. Uncertain market conditions will have an impact on company performance.

H6: Systematic risk has a significant negative effect on company performance. The higher the company's systematic risk, the lower the company's performance.

II. MATERIAL AND METHODS

The sample used in this study is that companies are consistently listed on the LQ45 index from 2014 to 2019 by 33 companies. The data used are 165 observation panel data. Use of companies listed in the LQ45 index considering that these companies are companies with the most liquid securities and relatively large trading volumes so that they can reflect the actual condition of the Indonesian Capital Market.

A. Measurement of Research Variables

1. Company performance (X1) is measured using Return on Assets (ROA) = Earning After Tax / Total Assets.
2. Systematic risk (X2) is measured by the beta (β) single index model concept. Beta (β) of each company is calculated by regressing each company's monthly stock returns with a monthly market return during the study period, with the function: $Ri = \alpha + \beta i\ (Rm) + e$.
3. Capital structure (X3) is measured by the Debt to Equity Ratio (DER).
4. Corporate value (Y) is measured by Tobin's Q which is calculated by adding up the debt market value (Debt = D) with the market value of its own capital (Market Value Equity = MVE) divided by total assets (Total Assets = TA); with functions: Tobin's Q = (MVE + D) / TA.

Data analysis method

This research analysis tool is Ordinary Least Square (OLS) regression and uses $\alpha = 0.05$. The regression function used is as follows.

Regression Model 1:

$Y = \alpha 1 + \beta 1X1 + \beta 2X2 + \beta 3X3 + e_1$

Regression Model 2:

$X3 = \alpha 2 + \beta 4X1 + \beta 5X2 + e_2$

Regression Model 3:

$X1 = \alpha 3 + \beta 6X2 + e_3$

III. RESULT

To test the hypotheses H1, H2, and H3, Regression Model 1 is used which is obtained from Table no 1:

$Y = \alpha 1 + \beta 1X1 + \beta 2X2 + \beta 3X3 + e_1$

$Y = 2.186 + 7.166X1 - 0.577X2 - 0.450X3 + e_1$

To test the hypotheses H4 and H5 used Regression Model 2 obtained from Table no 2:

$X3 = \alpha 2 + \beta 4X1 + \beta 5X2 + e_2$

$X3 = 0.137 - 0.038X1 - 0.034X2 + e_2$

To test the hypothesis H6 used Regression Model 3 obtained from Table no 3:

$X1 = \alpha 3 + \beta 6X2 + e_3$

$X1 = 0.418 - 0.642X2 + e_3$

From the classical assumption test results, all regression models are declared free from the problem of classical assumptions and fit so that it is feasible to be used as an analysis tool.

Tabel 1. Regression Coefficient Model 1:Company Performance, Systematic Risk, Capital Structure and Corporate Value

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	2.176	0.411		5.294	0.000
	Company Performance(X_1)	7.166	2.603	0.197	2.753	0.006
	Systematic Risk (X_2)	-0.577	0.236	-0.184	-2.446	0.015
	Capital Structure (X_3)	-0.450	0.226	-0.147	-1.992	0.047

a. Dependent Variable: Corporate Value (Y)

Tabel 2. Regression Coefficient Model 2:Company Performance, Systematic Risk and Capital Structure

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
2	(Constant)	0.137	0.004		38.877	0.000
	Company Performance(X_1)	-0.038	0.006	-0.351	-6.333	0.000
	Systematic Risk (X_2)	-0.034	0.005	-0.414	-6.800	0.000

a. Dependent Variable: Capital Structure (X_3)

Tabel 3. Regression Coefficient Model 3:Systematic Risk danCompany Performance

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
3	(Constant)	0.418	0.038		11,033	0.000
	Systematic Risk (X_2)	-0.642	0.043	-0.668	-14,930	0.000

Dependent Variable: Company Performance(X_1)

Testing H1: Company Performance (X1) has a significant positive effect on Corporate Value (Y) using regression model 1, whose output appears in Table no 1. From Table no 1, it appears that the Company Performance coefficient (X1) is 7,166 with a significance of 0.006 <α = 0.05, so H1 can be accepted. This means that the higher the Company Performance (X1), the higher the Corporate Value (Y).

Testing H2: Systematic Risk (X2) has a significant negative effect on Corporate Value (Y) using regression model 1, whose output appears in Table no 1. From Table no 1, it appears that the Systematic Risk (X2) coefficient is -0.577 with a significance of 0.015 <α = 0.05, so H2 can be accepted. This means that the higher the Systematic Risk (X2), the lower the Corporate Value (Y).

Testing H3: Capital Structure (X3) has a significant negative effect on Corporate Value (Y) using a regression model 1 whose output appears in Table no 1. From Table no 1, it appears that the coefficient of Capital Structure (X3) is -0,450 with a significance of 0.047 <α = 0.05, so H3 can be accepted. This means that the greater the funding comes from debt, the lower the Corporate Value (Y).

Testing H4: Company Performance (X1) has a significant negative effect on Capital Structure (X3) using regression model 2, whose output appears in Table no 2. From Table no 2, it appears that the coefficient of Company Performance (X1) is -0.038 with a significance of 0.000 <α = 0.05, so H4 can be accepted. This means that the greater the Company Performance (X1), the smaller the debt source.

Testing H5: Systematic Risk (X2) has a significant negative effect on Capital Structure (X3) using regression model 2, whose output appears in Table no 2. From Table no 2, it appears that the Systematic Risk (X2) coefficient is -0.034 with a significance of 0.000 <α = 0.05, so H5 can be accepted. This means that the greater the Systematic Risk (X2), the smaller the funding from debt.

Testing H6: Systematic Risk (X2) has a significant negative effect on Company Performance (X1) using regression model 3, whose output appears in Table no 3. From Table no 3, it appears that the Systematic Risk (X2) coefficient is -0,642 with a significance of 0,000 <α = 0.05, so H6 can be accepted. This means that the greater the Systematic Risk (X2), the lower the Company Performance (X1).

IV. DISCUSSION

A. Effect of Company Performance (X1) on Corporate Value (Y)

The influence of Company Performance on Corporate Value is evidenced by the acceptance of the H1 hypothesis, which states that the higher the Company Performance, the higher the Corporal Value. The results of this study are by some previous studies which have proven that company performance can directly improve corporate value[20],[21]. Signaling Theory that a high Company Performance will produce a high dividend to become an attraction for potential investors[25]. As a result, potential investors will hunt down the company's shares so that the company's stock price increases. The increase in the company's stock market price will have an impact on the Corporate Value increase.

B. Effect of Systematic Risk (X2) on Corporate Value (Y)

The result of hypothesis testing H2 proves that Systematic Risk has a significant negative effect on Corporate Value. The results of this study are consistent with the results of previous studies, which stated that high systematic risk would result in a decrease in corporate value[18]. Systematic risk is the risk that comes from external factors, so that it is uncontrollable. Systematic risk originates from market conditions and the economy in which the company operates[18]. These market and economic conditions affect all companies not to be eliminated by diversifying[26]. Companies have different sensitivity to economic conditions. Companies that have a high sensitivity to economic conditions will have a high systematic risk. The higher the systematic risk of a company, the less attractive it is to potential investors, thus impacting the decline in its stock market prices. Reducing the company's stock market price will result in a decrease in corporate value.

C. Effect of Capital Structure (X3) on Corporate Value (Y)

The hypothesis test H3 proves that the Capital Structure has a significant negative effect on Corporate Value. The results of this study are by several previous studies that have proven that capital structure has a significant negative effect on corporate value[12]. Using a capital structure in which the proportion is more debt than equity will cause a greater share of profits paid to creditors as interest payments so that net income to which shareholders are entitled to be less. As net income decreases, dividends paid out to shareholders are also getting smaller. According to the signaling theory, the decline in dividends becomes negative information for potential investors, causing a decline in the company's stock price[25]. A decline in the company's stock price

makes the corporate value go down. So, more use of debt than equity in capital structure will cause a decrease in corporate value.

D. Effect of Company Performance (X1) on Capital Structure (X3)

The results of hypothesis testing H4 prove that Company Performance has a significant negative effect on Capital Structure. The results of this study are by the Pecking Order Theory, which states that companies with high performance tend to use financing sourced from equity to finance new projects that can increase the corporate value[12]. The results of this study are also by some previous studies that have proven that company performance is negatively related to capital structure[13], [14], meaning that high-performing companies tend to use more sources of funding from equity than sources of funds debt. An optimal capital structure is one of the objectives of the company's financial policy. With an optimal capital structure, the company will have sufficient funds to fund development investment with minimal capital costs to improve the company's performance.

E. Effect of Systematic Risk (X2) on Capital Structure (X3)

The results of hypothesis testing H5 prove that Systematic Risk has a significant negative effect on Capital Structure. This means that the greater the systematic risk companies face, the more companies will use internal funding. Harry Markowitz (1952) has stated that investors face two risk groups, namely Systematic risk and unsystematic risk[22]. Systematic risk is the risk that comes from external factors, so that it is uncontrollable. This external condition affects all companies, so that it cannot be eliminated using diversification. Each company has a different sensitivity to external conditions. Companies that have a high sensitivity to external conditions will have a high systematic risk. The higher the systematic risk, encouraging companies to be more careful. Therefore companies with high systematic risk must reduce their debt[24]. The higher the systematic risk, the company tends to use more equity than the debt in its capital structure. The use of greater equity is intended to avoid the failure of interest payments. Failure to pay interest is categorized as a failure that can lead to bankruptcy demands by creditors.

F. Effect of Systematic Risk (X2) on Company Performance (X1)

The results of hypothesis testing H6 prove that Systematic Risk has a significant negative effect on Company Performance. The results of this study are consistent with the results of previous studies, which have proven that the more stable the external conditions will improve Company Performance[18]. The risk is divided into two, namely systematic risk and unsystematic risk[22]. Systematic risk is the risk that comes from external factors, especially from economic conditions. Therefore, systematic risk is also referred to as market risk. Because it is sourced from the company's external factors, the company can avoid systematic risk so that it always exists. Therefore investors in the capital market cannot avoid or reduce systematic risk by diversifying investment portfolios.

The companies that operate in an environment with uncertain market conditions will face serious problems. The company's sales are difficult to predict precisely. As a result, the company cannot predict the profit that will be obtained. Uncertain market conditions will have an impact on the decline in Company Performance.

G. Mediation Testing

To test the indirect effect of Company Performance (X1) and Systematic Risk (X2) on Corporate Value (Y) through Capital Structure (X3), and the indirect effect of Systematic Risk (X2) on Company Performance (X1) through Capital Structure (X1) X3) used path analysis using the Standardized Coefficients Beta and Analysis Model presented in Figure 1.

The indirect effect of Company Performance (X1) on Corporate Value (Y) through Capital Structure (X3) is β3 x β4 or -0.147 x -0.351 = 0.052. This multiplication result is smaller than the direct effect of Company Performance (X1) on Corporate Value (Y) shown by β1 = 0.197. So it can be concluded that the direct effect of Company Performance (X1) on Corporate Value (Y) is more effective than the indirect effect of Company Performance (X1) on Corporate Value (Y) through Capital Structure (X3).

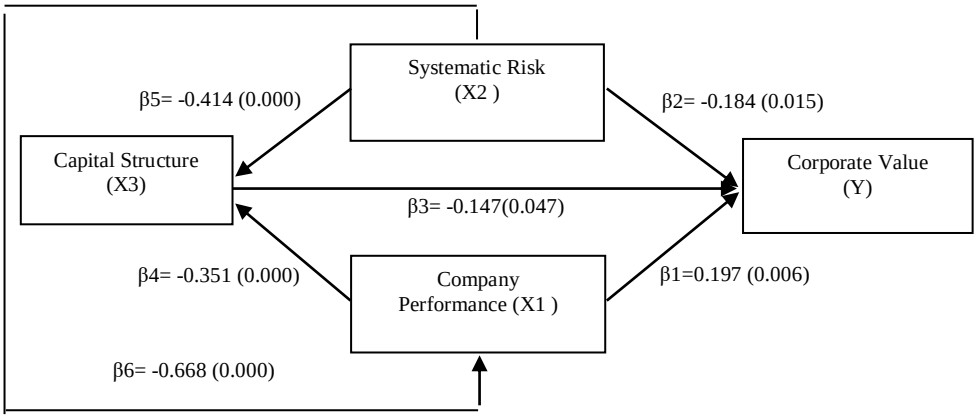

Fig. 1 Mediation analysis model

The indirect effect of Systematic Risk (X2) on Corporate Value (Y) through Capital Structure (X3) is β3 x β5 or -0.147 x -0.414 = 0.060. This multiplication result is smaller than the direct effect of Systematic Risk (X2) on Corporate Value (Y), which is indicated by the absolute value β2 = -0.184. So it can be concluded that the direct effect of Systematic Risk (X2) on Corporate Value (Y) is more effective than the indirect effect of Systematic Risk (X2) on Corporate Value (Y) through Capital Structure (X3). The indirect effect of Systematic Risk (X2) on Capital Structure (X3) through Company Performance (X1) is β4 x β6 or -0.351 x -0.668 = 0.234. This multiplication result is smaller than the direct effect of Systematic Risk (X2) on the Capital Structure (X3) shown by absolute β5 = -0.414. So it can be concluded that the direct effect of Systematic Risk (X2) on Capital Structure (X3) is more effective than the indirect effect of Systematic Risk (X2) on Capital Structure (X3) through Company Performance (X1).

V. CONCLUSION

Company Performance has a significant positive effect on Corporate Value, while Systematic Risk and Capital Structure have a partially significant negative effect on Corporate Value. Company Performance is the most dominant factor affecting Corporate Value, while Capital Structure is the weakest factor affecting Corporate Value.

Company Performance and Systematic Risk partially have a significant negative effect on Capital Structure. Compared with Company Performance, Systematic Risk is the more dominant factor affecting Capital Structure. Systematic Risk has a significant negative effect on Company Performance.

The direct effect of Company Performance on Corporate Value is more effective than the indirect effect of Company Performance on Corporate Value through Capability Structures. The direct effect of Systematic Risk on Corporate Value is more effective than the indirect effect of Systematic Risk on Corporate Value through Capital Structure. The direct effect of Systematic Risk on Capital Structure is more effective than the indirect effect of Systematic Risk on Capital Structure through Company Performance.

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