

# **CAPITAL STRUCTURE, PROFITABILITY, AND FIRM VALUE (STUDY IN LISTED COMPANIES ON INDONESIA STOCK EXCHANGE NON-CYCLICAL CONSUMER SECTOR FOR THE PERIOD 2016-2020)**

## **CAPITAL STRUCTURE, PROFITABILITY, AND FIRM VALUE (STUDY IN LISTED COMPANIES ON INDONESIA STOCK EXCHANGE NON-CYCLICAL CONSUMER SECTOR FOR THE PERIOD 2016-2020)**

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### **Abstract**

*This study aims to determine the effect of capital structure and profitability on firm value in the consumer non-cyclical sector listed on the Indonesia Stock Exchange for 2016 – 2020 periods. Capital structure is measured by Debt to Equity Ratio (DER), profitability is measured by Return on Equity (ROE), and firm value is measured by Price to Book Value (PBV). This study uses quantitative method with purposive sampling as method of selecting samples and 34 companies were selected as samples. There are 141 observations collected in this study. The data analysis is multiple linear regressions with IBM SPSS 26 as data processing. The results of this study indicate that partially capital structure had a negative effect on firm value and profitability had a positive effect on firm value.*

**Keywords:** Capital Structure, Profitability, Firm Value

### **1. INTRODUCTION**

In order to expand the business, many companies use IPO (Initial Public Offering) as the way to gain capital. In 2021, there are 54 new companies are listed in Indonesia Stock Exchange (idx.co.id, 2021), this condition makes competition between companies in Indonesia Stock Exchange getting tougher. Every public company competes each other to attract new investor and attempted to keep good relationship with investors. In terms to maximize investor's contentment, all public companies should keep their firm value in good condition. Invent satisfaction to shareholders is one of the company's purpose (Hakim and Sugianto, 2018).

Consumer non-cyclical sector is the newly formed sector classification by Indonesia Stock Exchange. This sector plays an important role in Indonesia's Gross Domestic Product (GDP). Business field like agriculture and fishing contribute 12,62% on GDP, food and beverages manufacturing contribute 6,61% on GDP (bps.go.id, 2022). Those business fields are covered in consumer non-cyclical sector. In capital market this sector also took an important part as well. Consumer non- cyclical sector is the sector with the second largest market capitalization (ojk.go.id, 2022), which means it can impact Indonesia Composite Index. In 2021, consumer non-cyclical index fell 16.04% (kontan.co.id, 2022) and it shows this sector has problem with firm value because stock price is the reflection of firm value. Firm value is the price that investor willing to pay if the company's shares are sold.

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In the last 5 years, research related to the effect of capital structure on firm value and the effect of profitability on firm value still shows different research results. Then the capital structure and profitability are also directly related to the use and management of funds from investor. This relationship is expected to affect the value of the company. So, this study is going to focus on discovering the effect of capital structure and profitability on firm value in consumer non-cyclical sector.

Capital structure is combination of equity, preferred stock, and debt (Brigham and Houston, 2014). A company is considered to have good capital structure if the capital structure can maximize the value of the company (Sumardika and Artini, 2020). There are many researches about the effect of capital structure to firm value before. Research from Setiawan et al (2021), Ramdhonah et al (2019), Sahara et al (2022), shows the result that capital structure has effect on firm value however research from Yulianti et al (2022), Dhani and Utama (2017), shows result that capital structure doesn't affect firm value.

Profitability is business's ability to generate net profit. A company can attract investor by making a consistent profit every year. Profitability is one of the most important things for investor to make investment decision. There are many researches about the effect of profitability to firm value before. Research from Yanti and Darmayanti (2019), Saputri and Giovanni (2021), shows the result that profitability has effect on firm value however research from Sari et al (2021), Farizki et al (2021), and Oktrima (2017), shows the result that profitability doesn't affect firm value.

Previous research of the capital structure and profitability on firm value show there are gap, thus it is necessary to make further research related to this problem.

## **2. LITERATURE STUDY**

### **Signaling Theory**

Signaling theory begins with the assumption of asymmetric information between two parties (individual or organizations). The corporate's management has more information related to the business prospect than the information held by investors (Brigham and Houston, 2019 : 32). Signaling theory encourages the management to provide information about company's financial statement to investors. The financial statement that the company published to the outsider is the signal. The outsider party which is investor will react the signal with two responds, the first one is the signal considered as good news or the signal is considered as bad news.

### **Capital Structure**

Capital structure is combination of total debt, preferred stock, and equity as corporate business funding to funds its ongoing operation (Brigham and Houston, 2019 : 4). Capital structure is important because it can directly affect the statement of financial position and at the end it can affect the firm value. An investor's decision to invest in a company can be influenced by company's capital structure. Capital structure is supposed to maximize the firm value by arranging the right decision of capital source.

### **Profitability**

The business ability to generate profit is profitability (Kasmir, 2016 : 196). How well a management operates the business can be show on profit that the company gain at the end. The business efficiency can be measured by profitability ratio. Investors interested in a company that have high ratio of profitability and consistent profit year by year. Profitability is one of the important matters toward investor's investment decision.

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## **Firm Value**

A company established to reach the goals, one of the goals is to maximize firm value. Firm value is investor perception about the company. Firm value will reflect on stock price, the higher the price of a stock the higher value of the company. Firm value is able to increase when the investors put their trust on the company and it depends on the company performance year by year.

## **Hypotheses Development**

### **The Effect of Capital Structure on Firm Value**

Signaling theory stated that a company with good prospect is prefer funding from debt to funding from issue stock (Brigham and Houston, 2019 : 500). Signaling theory explain that company can increase its debt because its business continuity is reliable. Companies that are able to generate profit tend to increase their debt because the additional interest expense from debt will be offset by the tax burden (Sudana, 2019 : 173).

According to research from Priyatama and Pratini (2021), capital structure affect positively to firm value on Infrastructure, Utility, and Transportation Companies. The investors trust that debt interest expense will reduce the tax burden. Although the debt increase but the level of use is still within the optimal limit, the risk of bankruptcy won't occur. The first hypothesis in this study:

H<sub>1</sub> : Capital structure has positive effect on firm value

### **The Effect of Profitability on Firm Value**

As stated in signaling theory, profitability affect positively to firm value. The main reason investor invest their money on a company is because they want profit, therefore investors are looking for profitable companies. Profitability is one the important matter to evaluate business performance Nguyen and Nguyen (2020).

According to research from Yulianti et al (2022), profitability has positive effect to firm value on food and beverages sub-sector manufacturing companies. This positive effect caused by increasing profitability is considered a good prospect for the company. This good prospect seized by investor as good news. The second hypothesis in this study:

H<sub>2</sub> : Profitability has positive effect on firm value

## **3. RESEARCH METHODOLOGY**

The types of this study is quantitative descriptive. The population in this study is companies listed on Indonesia Stock Exchange (IDX) under consumer non-cyclical sector during period 2016 to 2020. This study uses purposive sampling as sample collecting, and left 34 companies from 98 companies as sample data. Multiple regression analysis is used as an analytical technique in this study and IBM SPSS 26 as data processing.

### **Independent Variable (X)**

#### **Capital Structure (X<sub>1</sub>)**

Capital structure in this study is proxies by Debt to Equity Ratio (DER). DER describes the proposition of company's total liabilities and equity. DER formula is :

$$DER = \frac{\text{Total liabilities}}{\text{Equity}}$$

### Profitability (X<sub>2</sub>)

Profitability in this study is proxies by Return on Equity (ROE). ROE shows how effective are the use of equity to generate net income. ROE formula is :

$$ROE = \frac{Net\ profit}{Equity} \times 100\%$$

### Dependent Variable (Y)

#### Firm Value

Firm value is proxies by Price to Book Value (PBV). PBV formula is :

$$PBV = \frac{Market\ value\ per\ share}{Book\ value\ per\ share}$$

### Regression Model

The multiple regression equation model in this study is:

$$Y = \alpha + \beta_1 X_1 + B_2 X_2 + e$$

Where:

Y : firm value proxies by PBV

$\alpha$  : constant

$\beta_1$  : coefficient X<sub>1</sub>

$\beta_2$  : coefficient X<sub>2</sub>

X<sub>1</sub> : capital structure proxies by DER

X<sub>2</sub> : profitability proxies by ROE

e : error

## 4. RESULT AND DISCUSSION

### Descriptive Statistical Analysis

Statistics descriptive is needed to show the description of all data samples.

Table 1 Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
Capital Structure (X <sub>1</sub> )	170	.17	4.29	1.2246	1.01297
Profitability (X <sub>2</sub> )	170	.29	145.09	19.7008	26.31953
Firm Value (Y)	170	.29	82.44	5.0111	11.10937
Valid N (listwise)	170				

Source : Data Processed SPSS 26, 2022

Based on table 1 shows that the amount of data in each variables is 170, the minimum value of variable capital structure is 0.17, the maximum value is 4.29, mean is 1.2246 and standard deviation is 1.01297. The minimum value of variable profitability is 0.29, maximum value is 145.09, mean is 19.7008, and standard deviation is 26.31953. The minimum value of variable firm value is 0.29, maximum value is 82.44, mean is 5.0111, and standard deviation is 11.10937. Standard deviation is reflection of the mean deviation. If the value standard deviation is bigger than the value of Mean, it means the poor representation of the overall data, so there must be data outliers and these data outliers must be eliminated, otherwise if the value of standard deviation is smaller than

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the value of Mean, it means the Mean value can be used as a representation of the entire data. In variable capital structure, the value of standard deviation is almost the same value with Mean, which means the data in capital structure isn't representable yet. In variable profitability, the value of standard deviation is bigger than the value of Mean, which the data in profitability isn't representable so there are some data or observations must be eliminated, and in variable firm value, the data isn't representable because the value of standard deviation is bigger than the value of Mean.

## **Outlier Test**

In statistics descriptive test shows that the data in variable capital structure, profitability, and firm value aren't representable because of data outliers. Outlier is the data that has a value that is different from other observations. In order to make the data representable, some data must be eliminated. This study used Z score and casewise diagnostics as outlier test.

Testing using Z score, categorizing the values that included in data outlier is  $-2.5 > Z > 2.5$ . The result in outlier test using Z score shows that there are 14 observations must be eliminated. The data outlier as follows:

1. Observation-20, the Multi Bintang Indonesia Tbk has the z score of 3.79 on ROE (Variable Profitability) in 2016.
2. Observation-24, the Millennium Pharmacon Internasional Tbk has the z score of 2.85 on DER (Variable Capital Structure) in 2016.
3. Observation-33, the Unilever Indonesia Tbk has the z score of 4.41 on ROE and the z score 5.21 on PBV (Variable Firm Value) in 2016
4. Observation-53, the Midi Utama Indonesia Tbk has the z score 3.02 on DER in 2017.
5. Observation-54, the Multi Bintang Indonesia Tbk has the z score of 3.79 on ROE (Variable Profitability) in 2017.
6. Observation-67, the Unilever Indonesia Tbk has the z score of 4.39 on ROE and the z score 6.96 on PBV (Variable Firm Value) in 2017.
7. Observation-88, the Multi Bintang Indonesia Tbk has the z score of 3.23 on ROE (Variable Profitability) in 2018.
8. Observatio-92, the Millennium Pharmacon Internasional Tbk has the z score of 2.87 on DER (Variable Capital Structure) in 2018.
9. Observation-101, the Unilever Indonesia Tbk has the z score of 3.81 on ROE and the z score 3.66 on PBV (Variable Firm Value) in 2018.
10. Observation-122, the Multi Bintang Indonesia Tbk has the z score of 3.25 on ROE (Variable Profitability) in 2019.
11. Observation-126, the Millennium Pharmacon Internasional Tbk has the z score of 2.96 on DER (Variable Capital Structure) in 2019.
12. Observation-135, the Unilever Indonesia Tbk has the z score of 4.56 on ROE and the z score 5.01 on PBV (Variable Firm Value) in 2019.
13. Observation-160, the Millennium Pharmacon Internasional Tbk has the z score of 2.81 on ROE (Variable Profitability) in 2020.
14. Observation-169, the Unilever Indonesia Tbk has the z score of 4.76 on ROE and the z score 4.66 on PBV (Variable Firm Value) in 2020.

After eliminate outlier data with z score, leaving 156 observations as samples and turns out that's still not enough, there are still data outlier that have not been detected which

makes the data not normally distributed, so in this study used casewise diagnostics as second step to detect outlier.

Casewise diagnostics test is one of the test that can detect outlier and in this study, data with standard deviation smaller than -2.5 and bigger than 2.5 categorized as data outlier. The data outlier as follows:

Table 2 Outlier Test with Casewise Diagnostics (1)

<b>Casewise Diagnostics<sup>a</sup></b>				
Case Number	Std. Residual	Nilai Perusahaan	Predicted Value	Residual
13	3.007	13.04	7.0004	6.03963
44	4.565	16.13	6.9616	9.16842
75	2.511	12.20	7.1575	5.04251
82	2.525	7.02	1.9487	5.07129
144	5.221	14.26	3.7730	10.48699
a. Dependent Variable: Nilai Perusahaan				

Source: Data Processed SPSS 26, 2022

Based on table 2 shows that observation 13, 44, 75, 82, 144 are categorized as data outlier because the standard deviation of each observation is more than 2.5 and after eliminate these 5 observations the remaining sample is 151.

Table 3 Outlier Test with Casewise Diagnostics (2)

<b>Casewise Diagnostics<sup>a</sup></b>				
Case Number	Std. Residual	Nilai Perusahaan	Predicted Value	Residual
19	2.838	6.01	2.0521	3.95795
48	3.022	6.29	2.0747	4.21529
63	3.257	6.63	2.0865	4.54347
a. Dependent Variable: Nilai Perusahaan				

Source: Data Processed SPSS 26, 2022

Based on table 3 shows that observation 19, 48, 63 are categorized as data outlier because the standard deviation of each observation is more than 2.5 and after eliminate these 3 observations the remaining sample is 148.

Table 4 Outlier Test with Casewise Diagnostics (3)

<b>Casewise Diagnostics<sup>a</sup></b>				
Case Number	Std. Residual	Nilai Perusahaan	Predicted Value	Residual
32	2.940	4.96	1.2401	3.71992
137	2.789	5.50	1.9710	3.52896
a. Dependent Variable: Nilai Perusahaan				

Source: Data Processed SPSS 26, 2022

Based on table 4 shows that observation 32 and 137 are categorized as data outlier because the standard deviation of each observation is more than 2.5 and after eliminate these 2 observations the remaining sample is 146.

Table 5 Outlier Test with Casewise Diagnostics (4)

<b>Casewise Diagnostics<sup>a</sup></b>				
Case Number	Std. Residual	Nilai Perusahaan	Predicted Value	Residual
3	2.737	5.05	1.7752	3.27479
6	-2.621	.90	4.0362	-3.13618
88	2.564	5.46	2.3914	3.06859
a. Dependent Variable: Nilai Perusahaan				

Source: Data Processed SPSS 26, 2022

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Based on table 5 shows that observation 3, 6, 88 are categorized as data outlier because the standard deviation of each observation is more than 2.5 and after eliminate these 3 observations the remaining sample is 143.

. Table 6 Outlier Test with Casewise Diagnostics (5)

<b>Casewise Diagnostics<sup>a</sup></b>				
Case Number	Std. Residual	Nilai Perusahaan	Predicted Value	Residual
102	2.580	4.74	1.8706	2.86940
a. Dependent Variable: Nilai Perusahaan				

Source: Data Processed SPSS 26, 2022

Based on table 6 shows that observation 102 categorized as data outlier because the standard deviation of each observation is more than 2.5 and after eliminate this observations the remaining sample is 142.

. Table 7 Outlier Test with Casewise Diagnostics (6)

<b>Casewise Diagnostics<sup>a</sup></b>				
Case Number	Std. Residual	Nilai Perusahaan	Predicted Value	Residual
18	2.540	5.79	3.0241	2.76592
a. Dependent Variable: Nilai Perusahaan				

Source: Data Processed SPSS 26, 2022

Based on table 7 shows that observation 18 categorized as data outlier because the standard deviation of each observation is more than 2.5 and after eliminate this observations the remaining sample is 141.

## Classic Assumption Test

Table 8 One Sample Kolmogorov-Smirnov Test

<b>One-Sample Kolmogorov-Smirnov Test</b>		
		Unstandardized Residual
N		141
Normal Parameters <sup>a,b</sup>	Mean	.0000000
	Std. Deviation	1.05934217
Most Extreme Differences	Absolute	.085
	Positive	.085
	Negative	-.044
Test Statistic		.085
Asymp. Sig. (2-tailed)		.015 <sup>c</sup>
Exact Sig. (2-tailed)		.250

Source: Data Processed SPSS 26, 2022

Based on table 8, it shows exact sig. (2 –tailed) is 0.250, which means the value is greater than 0.05, and it explain that the data residual is normally distributed.

Table 9 Multicollinearity Test

		<b>Coefficients<sup>a</sup></b>					Collinearity Statistics	
		Unstandardized Coefficients	Std.	Standardized Coefficients	t	Sig.	Tolerance	VIF
Model		B	Error	Beta				
1	(Constant)	.794	.223		3.563	.001		
	Capital Structure	-.264	.106	-.160	-2.483	.014	1.000	1.000
	Profitability	.124	.013	.635	9.891	.000	1.000	1.000

a. Dependent Variable: Nilai Perusahaan

Source: Data Processed SPSS 26, 2022

Based on table 9, it shows tolerance of capital structure is 1, VIF is 1 and tolerance of profitability is 1, VIF is 1, to pass multicollinearity test required tolerance  $> 0.10$  and  $VIF < 10$  (Ghozali, 2018 : 108). The result explains that independent variables aren't correlated with one another.

Table 10 Heteroscedasticity Test

Variable	Sig. (2-tailed)	Description
Capital Structure	0,980	No Heteroscedasticity
Profitability	0,650	No Heteroscedasticity

Source: Data Processed SPSS 26, 2022

Based on table 10 sig. (2-tailed) capital structure is 0.980 and sig. (2-tailed) profitability is 0.650, which means in data sample isn't found variance inequality from the residual of one observation to another observation.

### Multiple Linear Regression Analysis

Table 11 Multiple Linear Regression

		<b>Coefficients<sup>a</sup></b>				
		Unstandardized Coefficients	Std. Error	Standardized Coefficients	t	Sig.
Model		B		Beta		
1	(Constant)	.794	.223		3.563	.001
	Capital Structure	-.264	.106	-.160	-2.483	.014
	Profitability	.124	.013	.635	9.891	.000

a. Dependent Variable: Nilai Perusahaan

Source: Data Processed SPSS 26, 2022

Based on table 11, the constant value is 0.794, the coefficient of variable capital structure ( $X_1$ ) is -0.264 and the coefficient of variable profitability ( $X_2$ ) is 0.124. The regression model equation will be as follows :

$$Y = 0.794 + (0.264)X_1 + (0.124)X_2$$

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## Hypothesis Testing

Table 12. F Test Results

ANOVA <sup>a</sup>					
Model		Sum of Squares	df	Mean Square	F
1	Regression	118.732	2	59.366	52.145
	Residual	157.109	138	1.138	
	Total	275.841	140		

a. Dependent Variable: Nilai Perusahaan

b. Predictors: (Constant), Profitabilitas, Struktur Modal

Source: Data Processed SPSS 26, 2022

F table on this test is 3.061. Based on table 12 f Value is 52.145, so f Value > f Table because 52.145 > 3.061 and sig shows 0.000 which is greater than 0.000. It means that capital structure and profitability simultaneously affect firm value.

Table 13. Coefficient Determinant Test

Model Summary				
Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.656 <sup>a</sup>	.430	.422	1.06699

a. Predictors: (Constant), Profitability, Capital Structure

Source: Data Processed SPSS 26, 2022

On table 6 shows that adjusted R square is 0.422 which means the ability of independent variable (capital structure and profitability) to explain the variability of independent variable (firm value) is 42.2% and the rest, 57.8% is explain by others factor.

Table 14. T Test Results

Coefficients <sup>a</sup>					
		Unstandardized Coefficients		Standardized Coefficients	
Model		B	Std. Error	Beta	t
1	(Constant)	.794	.223		3.563
	Capital Structure	-.264	.106	-.160	-2.483
	Profitability	.124	.013	.635	9.891

a. Dependent Variable: Nilai Perusahaan

Source: Data Processed SPSS 26, 2022

This study discuss 3 variables in it and the amount of sample is 141 data,  $\alpha = 5\%$  so t table on this study is 1.977. Based on table 7 shows the result of individual significance test for the variables in this study, the explanation of the results as follows:

a. Testing of hypothesis 1

On table 7 shows that capital structure t Value is -2.483, which means t Value > t Table, because  $-2.483 > 1.977$ , and sig value is 0.014 which is smaller than 0.05, but there is negative sign on capital structure, so even if capital structure does affect firm value, hypothesis 1 is rejected.

b. Testing of hypothesis 2

On table 7 shows that profitability t Value is 9.891, which means t Value > t Table because  $9.891 > 1.977$ , and sig value is 0.000 which is smaller than 0.00. This result shows that profitability does affect firm value with positive effect, and hypothesis 2 is accepted.

## DISCUSSION

### The Effect of Capital Structure on Firm Value

Based on the results of statistical data processing, it shows that capital structure (Debt to Equity Ratio) has negative effect on firm value (Price to Book Value) so the hypothesis 1 is rejected. The negative effect of capital structure to firm value has meaning that when the capital structure increases, the firm value will decrease and when the capital structure decrease, the firm value will increase. This study result isn't in line with Signaling Theory, where's this theory explain that the increase in debt as positive signal to investor. According to Anggraini and MY (2019), the higher use of debt could cause bankruptcy. To minimize the risk of bankruptcy in the company, the company needs to pay attention to the use of debt. The way to minimize this risk is to maintain the DER value bellow 1 but unfortunately MEAN value of DER in this study is above 1, so this makes investors hesitate to put their investment in the company and it affects firm value negatively. Capital structure is crucial thing in business, a company may fall if the management is wrong in managing the capital. Considering about this negative relation between capital structure (DER) and firm value (PBV), the company must maintain the value of DER bellow 1 and if it necessary to increase debt, the company should make sure the usage of debt will increase sales. The result of this study is in line with research from Anggraini and MY (2019) which states that capital structure affects negatively to firm value.

### The Effect of Profitability on Firm Value

Based on the results of statistical data processing, it shows that profitability (Return on Equity) has positive effect on firm value (Price to Book Value) so the hypothesis 2 is accepted. The positive relation between profitability and firm value explain that when profitability is rises the firm value will rises as well and when profitability decline the firm value will decline as well. This positive effect is caused by investors perception of a business with good profitability is good news. A high level of profit indicates that the company has bright prospects. Profitability is an important thing because it shows companies performance to generate profit and a company can gain investors trust with that. Profitability as measured by ROE shows how well management manages funds from investor to generate profit. The result in this study is in accordance with the Signaling Theory proposed in this study and in line with the research from Akbar and Fahmi (2020), Dhani and Utama (2017). A company with high and consistent

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profitability is investor's favorite. Think of this positive relation between profitability and firm value then it's a must for the company to keep their profitability at high level by increasing management quality.

## **5. CONSLUSION AND SUGGESTIONS**

### **CONCLUSION**

The result on this study shows that capital structure proxies by Debt to Equity Ratio (DER), does affect firm value proxies by Price to Book Value (PBV), but in negative way and profitability proxies by Return on Equity (ROE), does affect firm value in positive way. It can be concluded that if capital structure is increase then firm value will decrease and if capital structure is decrease the firm value will increase so therefore, companies should make wise policy to handle capital source for business activity, wrong decision can impact to firm value. The positive effect indicated by profitability to firm value, can be concluded that if profitability rises then the firm value will rises and if profitability decrease then firm value will decrease. Companies should put concern on management performance so that the business can generate high profit rate and increase the value of the company.

### **SUGGESTIONS**

1. Adding or using other factors for independent variables because in this study only uses 2 variables and there are many factors could affect firm value.
2. Use other measuring tools to measure capital structure and profitability; it can be Debt to Asset Ratio (DAR) and Return on Asset (ROA).
3. Try another sector or industry as object such as consumer cyclical sector, healthcare, technology, etc.

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