

Relationship Model of Capital Structure, Profitability and Profit Growth

Section:
Financial Management

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Abstract

This study aimed to determine the effect of capital structure and Profitability on profit growth. The sample collected secondary data from companies in the Food and Beverage Industry sub-sector listed on the Indonesia Stock Exchange. The sampling in this study used a purposive sampling method with the following criteria: (1) listed on the Indonesia Stock Exchange; (2) Issued audited financial statements for the period 2017-2019. The data needed in this study was taken from the Indonesia Capital Market Directory (ICMD) 2017-2019. Statistical tests were carried out with t-test and multiple linear regression analysis before this test, first the classical assumption test. The study results show that: Capital structure does not affect profit growth, while Profitability has a significant positive effect on profit growth.

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INTRODUCTION

Companies that succeed in obtaining maximum profits as targeted will tend to provide rewards for the welfare of owners, employees and improve product quality. According to the Journal (Gunawan and Wahyuni, 2013). Along with the pace of the world economic order, which has developed and led to a free-market financial system, companies are increasingly being pushed to improve competitiveness. Profit is generally used as a measure of achievement achieved by a company to be used as a basis for returns on investment decisions and predictions to predict future earnings changes. Profit is the excess of income over costs in return for producing goods and services during an accounting period. According to Wild and Subramanyam (2014), "Earnings or net income indicates the company's profitability. Earnings reflect returns to equity holders for the period, while items in the report detail how profits are earned. Profit growth is an increase in profit or decrease in profit per year. Profit growth can be used to assess how the performance of a company. According to Dewi Utari, Ari, and Darsono (2014) Stating that good company profit growth reflects that the company's performance is also good; if the economic conditions are good in general, the company's growth is good.

According to Fahmi (2014), the Solvency Ratio (Leverage Ratio) is a ratio used to describe the company's ability to fulfill and maintain its ability to meet its obligations in paying debts on time consistently. Companies with a high level of financial leverage can result in financial difficulties (financial distress) in settling their debt obligations (Lestari, 2017). According to Sudaryono (2017), this ratio is used to measure the company's ability to fulfill obligations, both short and long term. According to Sayekti and Saputra (2015), research revealed that the Debt to Equity Ratio simultaneously affects profit growth. The debt to Equity Ratio shows how much the company's capital is used to guarantee a debt. With a high debt value, the resulting profit will decrease. Therefore, the solvency ratio or leverage will affect profit growth. However, it is different from Andriyani's (2015) research, which shows that the Debt to Equity Ratio does not affect profit growth.

The most commonly used profitability ratio is the return on equity (ROE). This ratio shows the efficiency of the use of own capital. This means that the company owner's position is getting less potent, and vice versa. The return on investment shows the productivity of all company funds, an increase in loan capital, and own capital. The higher this ratio, the better, and vice versa. This ratio shows how the company manages its capital effectively, measuring the profit level from investments that the owners have made of their capital. (Cashmere 2019). The research results conducted by Syamni and Martunis (2013) concluded that return on equity has a significant effect on changes in profits for telecommunications companies on the Indonesia Stock Exchange. The research results by Lim, Kardinal, and Juwita (2013) conclude that: Return on Equity does not significantly affect the Profit Growth of consumer goods companies, Firmansyah and Mahardhika (2016) partially figure that ROE does not affect profit changes with the calculation results. Based on this phenomenon, this research aims to determine the effect of profitability and capital structure on profit growth.

LITERATURE REVIEW

Profit Growth

Profit growth is an increase in profit or decrease in profit per year. Profit growth can be used to assess how the performance of a company. According to the Indonesian Accounting Association (2009), "net income (profit) is often used as a performance measure or as a basis for other actions such as return on investment or earnings per share. Profit growth is essential

information for many people, including entrepreneurs, financial analysts, shareholders, economists, and so on. The primary purpose of earnings reporting is to provide helpful information to those most interested in financial statements. Profit growth from year to year is also used to measure management efficiency and helps predict the company's future direction or future dividend distribution. Profit growth will affect the investment decisions of investors and potential investors who will invest their capital in the company.

Capital Structure

The capital structure, according to (Fahmi, 2014) is divided into two: First, simple capital structure, namely if the company only uses its capital in its capital structure. Second, complex capital structure, namely if the company uses its own capital and uses borrowed money in its capital structure.

Profitability

According to Sutrisno (2012), profitability is the company's ability to generate profits with all the capital working in it. The growth of the company's profitability is one of the critical indicators for investors in assessing the company's prospects in the future. The higher the ability to earn profits, the greater the return expected by investors, thus making the company value better (Pamadanu, 2013). In this study, profitability will be measured using ROE (Return on Equity) because this ratio is used to measure the performance of the company's management in managing the available capital to generate profit after tax. The ROE ratio is the ratio of net income to common stock equity, which measures the return on investment of common stockholders.

METHODOLOGY

The research used in this research is causal associative research. Associative-causal is research that looks for the relationship between two or more variables. The purpose of associative research is to find the relationship between one variable and another. The population of this study is manufacturing companies in the food and beverage industry sector in Indonesia which are listed on the Indonesia Stock Exchange (IDX). A certain number of samples were taken from the existing population using the purposive random sampling technique, namely determining the sample with specific considerations (Suliyanto, 2005). The sample used in this study was selected based on the following criteria: (1). Manufacturing companies in the basic and chemical industry sectors listed on the IDX in 2017-2019; (2). the data owned by the company is complete and following the variables studied.

Data collection technique

The data used in this study is time-series or time-series data. According to Kuncoro (2009), time-series data is data that is arranged chronologically arranged according to time on a specific variable. This study uses time-series data on an annual basis from 2016 to 2018. The data collection method used in this study is the documentation method. The documentation method is carried out by collecting data from various literature according to the research theme and data from financial reports contained on the Indonesia Stock Exchange (IDX) during 2017-2019.

Measurement

Profitability is the company's ability to generate profits with all the working capital (Sutrisno, 2012:16). $ROE = (\text{Profit After Tax}) / (\text{Equity Capital})$. Capital Structure is the ratio between total debt and total equity (Fahmi, 2019). $DER = (\text{Total Accounts Payable}) / (\text{Total Equity})$. Company growth is an increase in profit from year to year or from time to time (Harahap 2010). $\text{Growth} = (\text{Profit } t - \text{Profit } t-1) / (\text{Profit } t)$

RESULTS AND DISCUSSION

Descriptive statistics

Data Descriptive statistics include minimum, maximum, mean, and standard deviation. The research variable data consists of the dependent variable, namely Capital Structure. and independent variables include liquidity, profitability, and company growth. The results of descriptive statistical analysis are shown in table 1:

Table 1.

Descriptive Statistics Results

	N	Minimum	Maximum	Mean	Std. Deviation
DER	216	,00	10,48	1,4053	1,55416
ROE	216	,00	1,36	,0708	,11485
GROWTH	216	,00	196,55	5,1848	22,69657
Valid N (listwise)	216				

Based on table 1 from the results of the descriptive output, it can be seen that the description of each variable: Capital structure The results of descriptive statistics from the data collected show that the independent variable as measured by Capital Structure has a minimum value of 0.00, while the maximum value of 10.48. The average value or mean obtained is 1.4053, with a standard deviation of 1.55416. 2. Profitability The independent variable of profitability as measured by Return on Assets (ROA) has a minimum value of 0.00, while the maximum value of 1.36. The average value obtained is 0.0708, with a standard deviation of 0.11485. 3. Profit Growth The dependent variable profit growth has a minimum value of 0.00, while the maximum value is 196.55. The average value obtained is 5.1848, with a standard deviation of 22.69657.

Hypothesis testing

Coefficient of Determination Test (R²)

This test shows the percentage of the independent variable's ability to explain the variation of the dependent variable. The magnitude of the coefficient of determination is from 0 to 1. The closer to zero the magnitude of the coefficient of determination, the smaller the influence of the independent variable. On the contrary, the closer to one the magnitude of the coefficient of determination, the greater the influence of the independent variable. The test results are shown in Table 2. The coefficient of determination of Adjusted R Square has a value of 0.219, so it can be stated that the ability of the independent variables (liquidity, profitability, and company

growth) in explaining the variation of the dependent variable (capital structure) is quite large, limited, because it is 64%. The R² value of the first hypothesis is 0.228, which means that the percentage of the contribution of the liquidity, profitability, and company growth variables is 22.8%, while other variables outside the model influence the rest (100%-22.8% = 78.2%). The goodness of Fit models Simultaneous significance test (F test) shows whether all independent variables included in the model have a common effect on the dependent variable. (Ghozali, 2009). If the F test analysis shows that all the independent variables are simultaneously a significant explanatory of the dependent variable.

Table 2.

Regression Analysis

Variable	B	SE	t	Sig
(Constant)	,742	,366	2,024	,044
DER	-,174	,257	-,677	,499
ROE	1,850	,820	2,257	,025
Adj. R square	0.219			
f-statistics	3.118			
Sig	0.000			

The effect of capital structure on profit growth

The regression coefficients in Table 2 show that the capital structure proxied by the debt to equity ratio has a negative t count of -0.677 with a probability of 0.499. The p-value (0.499) > the level of significance (0.05), so H1 is unacceptable, meaning that the capital structure has an insignificant effect on profit growth. These results indicate that the company's capital structure has no significant impact on the capital structure. The results of this study support previous research conducted by Dianitha et al. (2020), which states that there is no influence between the Debt to Equity Ratio on the company's profit growth. However, the results of this study do not support the results of research by Sayekti and Saputra (2015), which states that there is an influence between the Debt to Equity Ratio on profit growth. So, the hypothesis which states that the Debt to Equity Ratio (DER) variable affects earnings growth cannot be accepted.

The Effect of Profitability on Profit Growth

The regression coefficients in Table 2 show that profitability has a positive t count of 2.257 with a probability of 0.025; p-value (0.025) < significance level (0.05), so H2 is acceptable, profitability has a significant effect on profit growth. These results indicate that the magnitude of the company's profitability has a significant positive impact on profit growth due to the nature and pattern of investment made by the company being appropriate so that all assets are used efficiently to maximize the profit obtained. Thus, companies with high profitability ratios tend to have high-profit growth in consumer goods industry sectors. In addition, the owned capital is also used to cover the debts they have. This condition follows research conducted by Nikmah and Wahyuningrum (2020), which states that return on assets has a significant

positive effect that investors can use as a signal for increasing profits so that investors can plan future company strategies.

CONCLUSION

Based on the results of the analysis and discussion that has been done, it can be concluded that capital structure has no significant effect on profit growth. In contrast, profitability has a significant positive impact on profit growth. For future researchers, it is recommended that further researchers use more samples with more diverse characteristics from various industrial sectors and extend the research period. Other studies should also add independent variables that also affect profit growth.

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Declarations

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Data, Materials and/or Code Availability:

Data sharing is not applicable to this article as no new data were created or analyzed in this study.