

# The Influence of Investment Decision, Financing Decision, and Dividend Policy on Firm Value

## Study on Basic Industry and Chemical Sector Company Listed on Indonesian Stock Exchange from Years 2006-2015

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**Keywords:** Investment Decision, Financing Decision, Dividend Policy, Firm Value.

**Abstract:** This study aims to identify the influence of investment decision, financing decision, and dividend policy on firm value in basic industries and chemicals company listed in the Indonesia Stock Exchange (IDX) years 2006-2015. In this study, the investment decision was measured with Price Earnings Ratio (PER), while financing decision was measured by using Debt to Equity Ratio (DER), and dividend policy was calculated by employing Dividend Payout Ratio (DPR), meanwhile the firm value in this present study was examined by using Tobin's Q ratio. Purposive sampling utilized to determine the sample of the study. Statistical analyses used in this research were linier regression multiple with panel data. Based on regression significance test (F test) showed that regression model can be used to take a conclusion. Whereas, T-test result showed that investment decision has a positive influence on firm value, financing decision has a positive influence on firm value and dividend policy has an influence on firm value with negative direction.

## 1 INTRODUCTION

The company's goal in the long term is to maximize firm value. Maximizing firm value is a very important, because with increasing a firm value, the prosperity of the shareholders will increase also. Firm value is also seen to provide an overview of the actual company condition and is often used as a tools to influence investor's perspectives on company performance and company's prospect in the future. The ups and downs of firm value can be reflected from changes the stock prices in capital market, the higher stock price, the firm value will be higher too.

Firm value can be affected by financial decisions taken by company managers, such as: investment decision, financing decision, dividend policy. The financial decisions are intended to increase the prosperity of shareholders, which is shown by increasing firm value (Husnan and Pudjiastuti, 2012). In addition, the existence of financing decision making by the company can provide a signal to outsiders about company's condition. The signal sends information contained in each company's action, where such information was previously only known by company's management. Therefore, the

company must be wise and careful in determining these financial decisions, because the decisions can affect the firm value.

Basic industry and chemical sector is a sector that has many roles in proving the country's economy and stimulate the productivity of society and become a support in operational activities of other industries. Therefore, if a firm value in basic industry and chemical sector declines, it does not close the likelihood that it could affect in other sectors.

This study aims to determine: (1) The influence of investment decision on firm value. (2) The influence of financing decision on firm value. (3) The influence of dividend policy on firm value.

## 2 LITERATURE REVIEW

Harmono (2016) distinguishes financial management functions into three forms of corporate policy, namely (1) investment decision, (2) financing decision, (3) dividend policy. A financial manager must be able to optimize the three financial decisions to increase firm value or shareholder's wealth. Investment decision related to allocation of funds owned by the firm into

investment project that will be able to provide benefits for the firm. Investment decision is a very important decision in an effort to increase the firm value, because the investment decision has a big influence on company's development. With the right investment decision, the firm can give a new investment opportunities that give a profit to the firm, so the firm can increase shareholder's prosperity. In addition, investment decision have a long-term dimensions which can produce long-term consequences as well later.

Financing decision is related to selected of the right source of corporate funds that can provide optimal results for the firm, whether internal funds (equity) or external funds (debt). Use debt in financing decision can reduce the tax costs that must be borne by the firm (tax deductible) and can affect the investor's reaction. Investors will assume that the company is able to fund all company's activities and able to increase shareholder wealth. But on the other hand, excessive debt can reduce the firm value, because the higher debt can increase a interest expense and cause bankruptcy risk.

Dividend policy is a policy taken by the company's management to decide to pay a partly of a company's profit to the shareholders rather than hold it as retained earnings to be re-invested to obtain capital gains (Ambarwati, 2010). Dividends are earnings received by investors in the short-term and definitely accepted by investors, so dividend payments can reduce the investor's risk and can attract investors to invest in the company.

Bird in the hand theory suggests that dividend distributed by firms have a positive effect on stock price and firm value, but on the other hand tax preference theory suggests that investors prefer companies to hold most of their profits because the high dividends payout may result in greater tax payments. Other than that, any dividend policy taken by the company can affect the amount of company's retained earnings which will be used to fund company's investment activities. So in determining the dividend policy, finance manager should be consider the company's re-investment opportunities. The higher dividend can disrupt the firm expansion, while the lower dividend can reduce investor interest (Himawan and Cristiawan, 2016) therefore, dividend policy should be considered appropriately.

### 3 HYPOTHESIS

H<sub>1</sub>: Investment decision has a positive influence on firm value.

H<sub>2</sub>: Financing decision has a positive influence on firm value.

H<sub>3</sub>: Dividend policy has a influence on firm value

## 4 METHODOLOGY

### 4.1 Research Variable and Measurement

#### 4.1.1 Dependent Variable

##### a. Firm Value

Firm value is the price that the prospective buyer would pay if the company was sold (Husnan and Pudjiastuti, 2012) firm value can be measured using Tobin's Q ratio. Tobin's Q ratio is considered to provide the best information in measuring firm value. Because Tobin's Q ratio has included all debt and equity owned by the firm, so it can describe the ability of the firm in managing all assets.

$$\text{Tobin's Q} = \frac{(\text{EMV} + \text{D})}{(\text{EBV} + \text{D})} \quad (1)$$

#### 4.1.2 Independent Variable

##### a. Investment Decision

Investment decision are a matter of how financial manager should allocate funds into a investment project that will be profitable in the future (Sutrisno, 2012). Investment decision can be measured using Price Earnings Ratio (PER). PER is used to measure how investors assess a company growth prospect in the future, and reflected in the stock price that investors are willing to pay for each of the company's earnings (Sudana, 2011).

$$\text{PER} = \frac{\text{Market price per share}}{\text{Earning per share}} \quad (2)$$

##### b. Financing Decision

The financing decision addresses the problem of how much capital should be raised to fund the firm's operations (both existing and proposed), and what the best mix of financing is (Pike and Neale, 2009). So that a financial manager is required to determine the best composition of company's funds, namely funds in the form of debt and equity. Financing decision are measured using Debt to Equity Ratio (DER). Debt to Equity Ratio shows a comparison between debt and equity (Husnan and Pudjiastuti, 2012). The greater DER value shown the greater amount of debt usage in the company.

$$DER = \frac{\text{Total Debt}}{\text{Total Equity}} \quad (3)$$

### c. Dividend Policy

Dividend policy is decision related a distribution company profit, whether the profit will be distributed to shareholders or will be retained as retained earnings to finance future investment (Sartono, 2010). Dividend policy is measured using Dividend Payout Ratio (DPR). With using Dividend Payout Ratio can be known percentage of company earnings are distributed as dividend and retained as retained earnings.

$$DPR = \frac{\text{Dividend per Share}}{\text{Earning per Share}} \quad (4)$$

## 4.2 Population and Sample

In this research, the data used a secondary data from Indonesia Stock Exchange (IDX) and ICMD. Population in this research is a company in basic industry and chemical sector. The sample is chosen using purposive sampling method with the following characteristics: (1) basic industry and chemical company listing on Indonesia Stock Exchange on December 31, 2015, (2) published company financial report during 2006-2015 period and present it in Rupiah currency, (3) paid dividends at least once during 2006-2015 period.

## 4.3 Analysis Technique

To know the influence of each independent variable to dependent variable used multiple linier regression analysis with panel data. The analysis is conducted to determine the extent of influence given by independent variable to dependent variable if a number of independent variable more than one variable. This study was conducted using panel data. The linear regression equation in this model are:

$$Q = \beta_0 + \beta_{1it}PER + \beta_{2it}DER + \beta_{3it}DPR + \varepsilon_{it} \quad (5)$$

## 5 RESULTS

Pursuant to purposive sampling criterion, obtained the research sample counted 25 company, but 15 company have outliers data, so amount of research sample become ten company. After eliminating outliers data, research data has been problems of autocorrelation. Therefore it is necessary to heal by using the first difference method.

Panel data model selection used by Chow Test and Lagrange Multiplier Test. Common effect model

(pooled least square) was selected as estimation model.

Table 1: Calculating Result of F-test.

R-squared	0.969508
Adjusted R-squared	0.968444
S.E. of regression	0.294972
Sum squared resid	7.482725
Log likelihood	-15.77990
F-statistic	911.4744
Prob (F-statistic)	0.000000

Source: Output Eviews 9

Based on the result of data processing in Table 1, it's known that the F-statistic value is 911.4744 with significance level 0.0000. F-table at df numerator = 3 and df denominator = 86 with  $\alpha = 5\%$  is 2.71, so F-statistic > F-table and significance level < 0.05, it can be concluded that means of regression, so the equation model can used to make inferences about the effect of investment decision, financing decision, and dividend policy on firm value. R-squared value is 0.969508 shows that 96.95% of firm value is influenced by independent variables in the model.

Table 2: Multiple Regression of Panel Data Analysis Result.

Variable	Coefficient	Std. Error	t-Statistic	Prob.
C	-0.031372	0.031115	-1.008260	0.3162
D(PER)	0.992241	0.374248	2.651289	0.0095
D(DER)	0.371385	0.007110	52.23166	0.0000
D(DPR)	-0.036038	0.008445	-4.267418	0.0001

Source: Output Eviews 9

## 5.1 The Influence of Investment Decision on Firm Value

The result of regression analysis shows the value of t-statistic of investment decision of 2.65 > t-table 1.66277 with significance level 0.0095. The value of t-statistic > t-table, then Hypothesis 1 accepted, investment decision has a positive influence in firm value. Investment decision have a coefficient of 0.992241 on firm value, so if the investment decision increases by one unit, then firm value will also increases by 0.992241 units.

The influence of investment decision on firm value is the result of the investment activity itself. This is because every investment decision taken by the company can determine company's obtained profit and show the optimal performance. Investment decisions are very important, because the mistake in investment selection can disrupt company's sustainability. Therefore, financial managers must

maintain corporate investment development to achieve corporate objectives.

In addition, the existence of investment expenditure by the company can provide a positive signal (good news) for investors, that the company has good revenue growth in the future and can increase the shareholder's prosperity. This makes investors more interested and trust with company's prospect, so that investors more appreciate the value of the company's stock and firm value will be higher. The results of this study support previous research conducted by Mursalim et al. (2015), Efni et al. (2012), Prapaska and Muthmainah (2012), Clementin and Priyadi (2016), Wijaya et al. (2010), Alipudin et al. (2014) which state that investment decision have a positive influence on firm value.

## 5.2 The Influence of Financing Decision on Firm Value

Financing decision variable has t-statistic is 52.23166 with significance level 0.0000. the t-statistic value > t-table is 1,66277, then hypothesis 2 is accepted, so the financing decision has a positive influence on firm value. The financing decision has a coefficient of 0.371385, meaning that if the financing decision increases by one unit, then firm value will increases by 0.371385 units.

The positive influence of financing decision on firm value is suspected by debt usage can be used as a deduction of tax payment. In addition, high debt usage is a positive signal for investors that the company is able to fund all of its investment activities and expected to improve the company's prospects and be able to pay its obligations to shareholders, so that the prosperity of shareholders or firm value increases.

In trade-off theory, using debt can increase firm value to a certain optimum point, but if the amount of debt has exceeded the optimum point then the debt can reduce firm value. Based on the results of this research and trade off theory, it can be seen that financing decision applied by the average company of basic industry and chemical sector has not reached its optimum point, so that financing decision on the basic industry and chemical sector has a positive influence on the firm value. The results of this study support previous research by Wijaya et al. (2010), Hoque et al. (2014), Mursalim et al. (2015), Himawan and Cristiawan (2016), Chowdhury and Chowdhury (2010), Efni et al. (2012) and Rehman (2016) which states that financing decision has a positive influence on firm value.

## 5.3 The Influence of Dividend Policy on Firm Value

Dividend policy variable has t-statistic of -4.267418 with significance level 0.0001. The significance level  $< \alpha$  0.05 then hypothesis 3 is accepted, so dividend policy has an influence on firm value, but the influence indicates a negative effect. Dividend policy has a negative coefficient of -0.036038 it means that if the dividend policy increases by one unit, then firm value will decrease by 0.036038 units.

The negative influence in dividend policy variable is assumed that the high dividend payout can cause the less amount of retained earnings. It may cause the company have insufficient funds experience to funding its investment and operational activities in the future. Increased dividends can be bad news because it is suspected that the company has reduced its investment plant which will subsequently affect the investor's perspective on firm value (Haruman, 2008). Investors assume that the greater dividends are distributed to shareholders, the growth of investment will be hampered and can lower firm value. In addition, the tax preference theory states that investors prefer if the company retained the profits, because dividend income is taxed higher than capital gains and the capital gain can make investors delay the payment of taxes, because the tax of capital gains will be collected if the shares are sold, but the tax of dividend must be paid when the dividend is distributed.

Dividend policy in one side may reduce investor risk, but in other side a higher dividend policy can reduce the amount of retained earnings. The result of this study support previous research by Clementin and Priyadi (2016) and Haruman (2008) which states that the dividend policy has an influence on firm value with a negative influence.

## 6 CONCLUSIONS

Based on the results in this research, it can be made the following conclusions: (1) Investment decisions has a positive influence on firm value. (2) Financing decision has a positive influence on firm value. (3) Dividend policy has an influence on firm value with a negative direction. Further research is suggested to examine other sectors or use different analytical techniques and consider external factors that may affect firm value, such as interest rates, inflation rate, currency exchange rate, and others as an independent variable.



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