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The Relationship Between Ownership Structure, Capital Structure, and Firm Performance: The Evidence From Indonesian Manufacturing Sector

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Abstract: The manufacturing sector listed on the Indonesia Stock Exchange (IDX) has experienced a decline in performance that could be attributed to its ownership structure. Besides, Indonesian manufacturing companies rank highly among foreign debt borrowers, with a total debt of US$ 392.6 billion, as reported by Bank Indonesia's Foreign Debt Statistics (SULNI) emphasizing the importance of analyzing their capital structure to understand their financial health, as it is influenced by their debt and capital holdings. This study aims to thoroughly examine the pivotal roles of ownership structure and capital structure in shaping the future trajectory of companies in Indonesia's manufacturing sector, with a specific focus on how their financial decision-making affects their performance. This study analyzed data from 97 listed companies on the IDX over five years (2017-2021) using a statistical method called panel regression. The findings indicate that the way a company is owned does not significantly influence its performance. However, the study does uncover that capital structure, measured by DAR, negatively impacts ROA without affecting ROE. On the other hand, the capital structure measured by DER negatively impacts ROE without affecting ROA. Firm size plays a significant and positive role in influencing company performance as a control variable.
Keywords: Capital Structure; Firm Performance; Ownership Structure

INTRODUCTION

The current surge in the economy is a pivotal factor that necessitates companies to implement strategic measures to enhance their corporate value, which reflects their overall position and condition. An efficient strategy to achieve this goal is to optimize the utilization of the financial management function, whereby the financial decisions and policies enacted by the company's management can influence other financial decisions and play a substantial role in shaping the overall performance of the company. This enables companies to optimize their value and achieve their financial objectives as desired (aliyah & Herwiyanti, 2020).

Financial performance entails an estimation of the operational efficiency and productive capacity gauged through the scrutiny of financial statements and managerial achievements of an organization (Candy et al., 2022) The operational effectiveness of a company can be assessed through its profitability ratio, which indicates the level of profit or earnings obtained during a certain period and impacts investor trust in the company's prospects. To achieve optimal company performance, the company needs to maintain a balance between high liquidity, profitability, solvency, and activity ratios as these four ratios are interrelated (Batrancea, 2021). On the other hand, low values of these ratios may indicate poor or weak company performance.

Gauging the performance of a company can be achieved by analyzing profitability ratios, such as return on assets (ROA) and return on equity (ROE) (Ghardallou & Alessa, 2022). ROA serves as a metric to gauge how effectively and efficiently a company is utilizing its assets to generate post-tax profits, with higher ROA values indicating greater efficiency in creating profitability. On the other hand, ROE measures the level of profitability based on the equity invested by shareholders and portrays the financial performance and potential of the company to generate net income. A higher

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ROE is likely to attract investors due to the potential for substantial returns on their investments.

The ownership structure of a company has been demonstrated to exert a significant influence on overall company performance, in a study undertaken by (Queiri et al., 2021). It is a critical factor that plays a pivotal role in shaping company performance, influenced by various ownership types including managerial, institutional, government, and foreign ownership. Dakhlallh et al. (2021) unveil that managerial ownership (MO) has effects on company performance, encompassing both profitability and losses. Shareholders with substantial holdings are associated with higher investment potential and productivity. The extent of institutional ownership (IO) is evaluated based on the proportion of shares held by institutional investors, with institutional entities often holding a majority of long-term shares. Government ownership (GO) has also been identified as a factor that can impact a company's future performance (Tebourbi et al., 2020), influencing strategic decisions, resource allocation, and operational management, all of which can impact company performance. Foreign ownership (FO) also has the potential to enhance a company's customer base and operational effectiveness (Nguyen et al., 2020). Nevertheless, the correlation between FO and company performance can vary across different countries, necessitating further in-depth research to uncover these differences. In addition to ownership structure, a company's capital structure can also impact its performance.

Companies need to establish an effective capital structure to enhance performance, maximize value, and navigate external competition. Conversely, an inefficient capital structure can adversely impact business performance, firm value, and bankruptcy risk. Leverage refers to a company's capacity to meet all its obligations while maintaining a proportionate mix of equity and debt (Sepriani & Candy, 2022). Hence, companies can utilize the debt-to-assets ratio (DAR) and debt-to-ratio (DER) to gauge their capital structure. DAR evaluates the ability of a company's assets to meet its debt obligations (Ajmadayana et al., 2022). A high DAR ratio places a significant burden on a company's liabilities, potentially eroding its creditworthiness, as investors may question its ability to meet financial obligations with its assets. On the other hand, DER aids debtors and investors in assessing the financial risk of the company and allocating funds accordingly.

The manufacturing industry, previously considered stable economically with potential for future growth, currently is encountering challenges due to a decline in performance. This can be observed from data during the 2019-2021 research period at IDX, which shows a decrease in the performance of manufacturing companies (Jati & Jannah, 2022). Moreover, data from the Foreign Debt Statistics (SULNI) published by the Bank of Indonesia reveals that manufacturing companies currently hold the third position in terms of foreign debt ownership, with an increasing total compared to the previous period (US$ 392.6 billion as opposed to US$ 390.2 billion previously). Hence, it is crucial to take into consideration the capital structure of manufacturing companies, as it is impacted by their debt and capital holdings.

It is imperative to conduct rigorous and comprehensive research to thoroughly investigate and understand the intricate relationship between ownership structure and capital structure, and their potential effects on the performance of manufacturing companies listed in the IDX (Indonesia Stock Exchange).

The level of MO in a company can be assessed by examining the distribution of management and executive positions among board members. According to Hossain et al. (2021), higher managerial ownership can help resolve conflicts and improve productivity, resulting in better outcomes and larger incentives for owners. Studies by Dakhlallh et al. (2021); Khan et al. (2020); and Alabdullah (2018) present evidence that

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higher levels of MO contribute positively to the firm performance by reducing agency costs and improving operational efficiency. Competent managers who generate profits for their wealth are associated with enhanced company performance and market value. Furthermore, owners' rights to company assets incentivize investment in successful projects and active participation in management decisions (Siddique et al., 2022).

Large organizations' ownership of shares such as businesses, known as institutional ownership, can drive company performance improvement by reducing agency costs and overseeing management. Hossain et al. (2021) highlight IO's effectiveness in bearing monitoring costs and participating in board decision-making, leading to improved company performance. According to research by Nugroho and Widiasmara (2019); Novilia and Rasyid (2022); and Anggara and Muid (2021), institutional ownership positively influences company performance through effective external monitoring, resulting in improved performance.

In economically developing countries, GO is necessary to stimulate economic and financial development and foster growth (Dakhlallh et al., 2021). Studies by Dianitasari and Hersugondo (2020); Hunardy and Tarigan (2017); and Sihombing and Akbar (2022) suggest a favorable correlation between the proportion of GO and the performance of the company. GO in an organization serves as a supervisory mechanism to enhance organizational management, contributing to improved company performance through better information disclosure (Anggreni & Robiyanto, 2021).

FO has the potential to help companies grow their customer base and operate more effectively. Foreign investors are considered more skilled in reducing agency issues and mitigating the opportunistic behavior of managers across diverse national and cultural settings (Sobhan, 2022). However, research by Zraiq and Fadzil (2018) suggests that local investors may have better access to financial information compared to foreign investors who may have limited information and come from more transparent regimes. Studies by Alabdullah (2018); Anisah and Hartono (2022); and Ivan & Raharja (2021) also acknowledge a favorable correlation between FO and firm performance.

The long-term success of a company can be influenced by its DAR, which indicates how much of its resources rely on debt as a source of financing. Excessive DAR increases the risk of bankruptcy due to financial obligations. A low DAR is a positive sign, indicating a small portion of assets is funded by debt. Higher revenue or profit can be achieved if interest and principal payments are smaller than the amount borrowed. Liando (2021) shows that DAR hurts business success, while studies by Krisyadi and Rionaldo (2021); Rahman (2020); and Wahyuni (2022) found substantial positive impacts. However, Istan (2018) contradicts these findings, as it did not find a substantial impact on firm performance.

Debt financing constitutes a crucial component of a company's overall capital structure and has the potential to affect its profitability (Purwanti, 2020). Lower levels of borrowing and higher equity capital can result in lower interest payments, potentially leading to higher net profit for the company. On the other hand, if a company heavily relies on borrowing, higher interest expenses may erode the net profit. Drawing from the findings of the research carried out by Gunawan et al. (2022); Hidayat et al. (2022); and Wiranawata (2022), it is suggested that DER serves as a favorable indicator of capital structure that can positively impact company performance. However, there are contrasting findings from other studies, including those by Ghardallou (2022); Irman et al. (2020); and Sukesti et al. (2021). which indicate that DER may have a detrimental effect on company performance.

The hypothesis of the study is developed based on the comprehensive background information and identified issues mentioned above.

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H_1: Higher managerial ownership leads to higher firm performance.
H_2: Higher institutional ownership leads to higher firm performance.
H_3: Higher government ownership leads to higher firm performance.
H_4: Higher foreign ownership leads to higher firm performance.
H_5: A higher debt-to-asset ratio increases firm performance.
H_6: A higher debt-to-equity ratio increases firm performance.

METHODS

The research in this study focused on Indonesian manufacturing firms that are publicly listed on the IDX, specifically in three subsectors: the basic and chemical industry, various industries, and the consumer goods industry, totaling 171 companies. A purposive sampling method was utilized to carefully select 97 companies as the sample for this study, guided by specific research criteria outlined in Table 1.

Table 1. Criteria for Research Sample

Information	Amount
Manufacturing sector companies listed on IDX	171
Companies conducting IPOs after 2017	(41)
The company's annual reports inadequate	(10)
Company's financial statements in non-rupiah currencies	(23)
Sample companies meeting research criteria	97
Total of samples for 5 years (2017-2021)	485 sample

Source: Processed Data (2023)

This study makes use of secondary data to fully meet its research needs. Secondary data comprises information that has been gathered and made available by external sources, other than the researcher (Haralayya, 2021). For this research, the secondary data utilized include the annual reports of companies that are listed on the Indonesia Stock Exchange, covering the period from 2017 to 2021. These reports were sourced from the official website of the IDX.

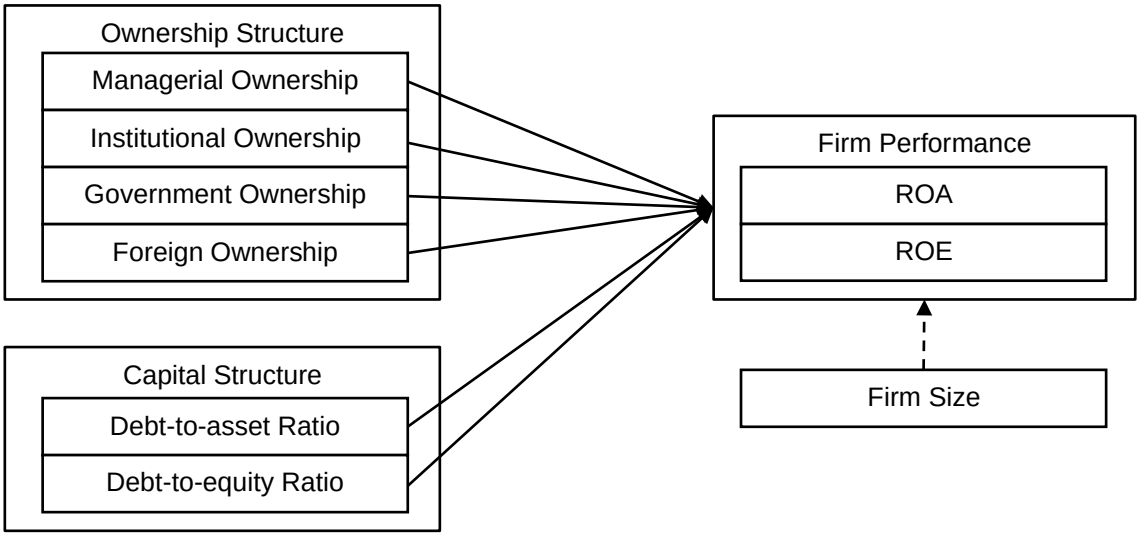

Figure 1. Schematic Framework
Source: Processed Data (2023)

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This study employs a causal approach to explore the relationships between variables by testing hypotheses and evaluating their interrelationships (Leksono & Pratiwi, 2022). Therefore, this study will examine the direct effects of the independent variables, specifically ownership structure and capital structure, on the dependent variable of company performance. Table 2 showcases the variables utilized in the research, along with the corresponding formulas conducted as part of the study.

Table 2. Measurement of the Variables

Variable Type	Variable Name	Measurement	Formula	Source
Dependent	Firm Performance	Return on Asset Ratio	$\frac{\text{Net Income}}{\text{Total Asset}}$	Ramzan *et al*. (2021)
		Return on Equity Ratio	$\frac{\text{Net Income}}{\text{Total Equity}}$	
Independent	Ownership Structure	Managerial Ownership	$\frac{\text{The percentage held by management}}{\text{Total Outstanding Shares}}$	Haryanto (2022)
		Institutional Ownership	$\frac{\text{The percentage held by institutional}}{\text{Total Outstanding Shares}}$	
		Government Ownership	$\frac{\text{The percentage held by the government}}{\text{Total Outstanding Shares}}$	
		Foreign Ownership	$\frac{\text{The percentage held by foreign}}{\text{Total Outstanding Shares}}$	
	Capital Structure	Debt-to-asset Ratio	$\frac{Total\ Liabilities}{\text{Total Asset}}$	Wiranawata (2022)
		Debt-to-equity Ratio	$\frac{Total\ Liabilities}{\text{Total Equity}}$	
Control	Firm Size	Firm Size	Log of Total Assets	Boulhaga *et al* 2022)

Source: Processed Data (2023)

The data collected for this study is categorized as panel data, as it encompasses both cross-sectional and time-series data. Thus, the E-Views program will be utilized to test the direct effect. The equation model used in this research is presented as follows:

$$Y = \alpha + \beta_1 X_{1it} + \beta_2 X_{2it} + \beta_3 X_{3it} + \beta_4 X_{4it} + \beta_5 X_{5it} + \beta_6 X_{6it} + \beta_7 Z_{1it} + \varepsilon$$

Where:
Y = Dependent variable
X = Independent variable
Z = Control variable
α = Constanta
β = Coefficient beta
ε = Error term
i = Cross-section item
t = Time series item

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RESULTS AND DISCUSSION

The descriptive statistical test yields several key outcomes that provide information about the distribution and variability of the sample data. These outcomes include the minimum and maximum values, the average values, and the standard deviation values. By analyzing these outcomes, the study can obtain information on how closely or distantly the data points are from the mean.

Table 3. Descriptive Statistical Test Result

Variable	Descriptive Statistic			
	Min	Max	Mean	Std. Dev
MO	0	9692,22360	82,85052	823,60794
IO	0	6,89972	0,62033	0,61716
GO	0	0,90025	0,27227	0,13119
FO	0	7,90000	0,26272	0,50908
DAR	-1,02693	2,89987	0,45470	0,31411
DER	-30,15344	114,28958	1,18361	5,81191
ROA	-1,04984	0,92100	0,04743	0,11955
ROE	-3,40794	4,90481	0,08783	0,40793
FS	25,21557	35,72132	28,69119	1,82684

Source: Processed Data (2023)

The data presented in Table 3 reveals several key findings. Firstly, the MO variable shows a narrow distribution, with the highest value recorded as 9692.22360 the lowest value as 0.00000, and an average of 82.85052. Meanwhile, the variability of the IO variable is low, as evidenced by its small standard deviation of 0.61716, and an average of 0.62033 with a minimum and maximum value of 0.00000 and 6.89972, respectively. The majority of FO shows that domestic investors hold shares in most companies, with an average value of 0.26272 and a range from 0.00000 to 7.90000. The variability of the GO variable is also low, with an average of 0.27227, a standard deviation of 0.13119, and minimum and maximum values of 0.00000 and 0.90025, respectively. In addition, the variable measuring the capital structure using DAR shows that PT Semen Indonesia (Persero) Tbk. has a minimum value of -1.02693 and a maximum value of 2.89987. The average DAR value is 0.45470, indicating that the company's debt level is generally higher than its assets. Another variable used to measure capital structure is DER. PT Asia Pacific Investama Tbk. holds the highest and lowest values for DER, with a maximum value of 114.28958 and a minimum value of -30.15344. The calculated average DER is 1.18361, with a standard deviation of 5.81191, indicating limited diversity in the DER data. The control variable of Firm Size (FS) has a maximum value of 35.72132 and a minimum value of 25.21557. The standard deviation of the FS variable is 1.82684, suggesting that the sampled companies have relatively high average asset sizes. Table 3 also shows that the sampled manufacturing companies have an average ROA of 0.04743 or 4.743% and an average ROE of 0.08783 or 8.783%. These average values of ROA and ROE indicate that manufacturing companies are proficient in effectively utilizing their assets and capital to generate profits for their shareholders.

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To ensure the accuracy and comprehensiveness of research results, it is imperative to conduct multiple tests to identify the most suitable model that aligns with the research data. These tests include Lagrange multiplier tests, Hausman tests, and Chow tests.

Table 4. Chow Test

Dependent Variable: Firm Performance (ROA)			
Independent Variables: Ownership Structure and Capital Structure			
Effect Test	**Statistic**	**d.f.**	**Prob**
Cross-section F	4,168361	(96,381)	0,0000
Cross-section Chi-Square	348,222271	96	0,0000
Dependent Variable: Firm Performance (ROE)			
Independent Variable: Ownership Structure and Capital Structure			
Effect Test	**Statistic**	**d.f.**	**Prob**
Cross-section F	2,090657	(96,381)	0,0000
Cross-section Chi-Square	205,232949	96	0,0000

Source: Processed Data (2023)

Table 4 presents the findings of the redundant fixed effect test, which investigates the impacts of the variables examined in the study. This test was conducted to ascertain the regression model that best elucidates the association between CEM and FEM. The results indicate that all probabilities linked to the relationship between ownership structure and capital structure on ROA and ROE are statistically significant. Next, the Hausman test will be shown in Table 5.

Table 5. Hausman Test

Dependent Variable: Firm Performance (ROA)			
Independent Variables: Ownership Structure and Capital Structure			
Test Summary	**Chi-Sq Statistic**	**Chi-Sq. d.f.**	**Prob.**
Cross-section random	6,138458	7	0,5237
Dependent Variable: Firm Performance (ROE)			
Independent Variables: Ownership Structure and Capital Structure			
Test Summary	**Chi-Sq Statistic**	**Chi-Sq. d.f.**	**Prob.**
Cross-section random	13,496309	7	0,0609

Source: Processed Data (2023)

Table 5 displays the results of the Hausman test, revealing that the probabilities associated with the impact of ownership structure and capital structure on ROA (0.5237) and ROE (0.0609) are both higher than the significance level α (α = 0.05). This suggests that the REM may be more appropriate to use compared to the FEM, as the probability value for random cross-section is above α. Thus, to determine the most effective model between the CEM and REM, the Lagrange multiplier test will be shown in Table 6.

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Table 6. Lagrange Multiplier Test

Dependent Variable: Firm Performance (ROA) Independent Variables: Ownership Structure and Capital Structure			
	Test Hypothesis		
	Cross-section	**Time**	**Both**
Breusch-Pagan	139,0865 (0,0000)	3,589456 (0,0581)	142,6759 (0,0000)
Dependent Variable: Firm Performance (ROE) Independent Variable: Ownership Structure and Capital Structure			
	Test Hypothesis		
	Cross-section	**Time**	**Both**
Breusch-Pagan	24,24452 (0,0000)	1,460262 (0,2269)	25,70478 (0,0000)

Source: Processed Data (2023)

Table 6 showcases the outcomes of the Lagrange Multiplier test. If the Breusch-Pagan cross-section value exceeds α (α = 0.05), CEM may be considered a viable option. On the other hand, if the value falls below α (α = 0.05), REM may be preferable. Since all the values in Table 6 are lower than α (α = 0.05), REM is considered the most favorable model to employ. Table 7 exhibits the findings of the regression test performed employing REM.

Table 7. Regression Test Results

Dependent Variable: Firm Performance (ROA)				
Variable	**Coefficient**	**Std. Error**	**t-Statistic**	**Prob.**
C	-0.298187	0.128256	-2.324940	0.0205
MO	7.805057	9.539776	0.818159	0.4137
IO	-6.560332	0.009565	-0.006859	0.9945
GO	0.010050	0.050364	0.199557	0.8419
FO	-0.002357	0.010533	-0.223788	0.8230
DAR	-0.133586	0.018591	-7.185326	0.0000
DER	0.000477	0.000740	0.644039	0.5199
FS	0.014135	0.004457	3.171190	0.0016
Dependent Variable: Firm Performance (ROE)				
Variable	**Coefficient**	**Std. Error**	**t-Statistic**	**Prob.**
C	-0.746625	0.318392	-2.344984	0.0194
MO	1.036114	2.382849	0.434821	0.6639
IO	0.024683	0.029902	0.825480	0.4095
GO	-0.125003	0.140111	-0.892170	0.3728
FO	-0.019775	0.034890	-0.566788	0.5711
DAR	0.081232	0.055276	1.469561	0.1423
DER	-0.038426	0.002526	-15.21349	0.0000
FS	0.029118	0.011057	2.633469	0.0087

Source: Processed Data (2023)

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The test results in Table 7 reveal that DAR has a noteworthy detrimental influence on ROA, as indicated by the exceedingly low probability value of 0.0000 and a coefficient of -0.133586. Conversely, the findings suggest that firm size exerts a considerable favorable effect on ROA, with a probability value of 0.0016 and a coefficient of 0.014135. Moreover, DER significantly and adversely impacts ROE, with a probability value of 0.0000 and a coefficient of -0.038426. Additionally, the study uncovers a significant positive impact on ROE about firm size, with a probability value of 0.0087 and a coefficient of 0.029118.

Hypothesis Testing (H_1)

The examination of the impact of MO on firm performance, as examined with ROA and ROE, was found to be insignificant. Descriptive results revealed that MO averaged 8285.052%, indicating a high level of ownership by the management in the company. This suggests that when management holds significant shares, they may be inclined to prioritize decisions that benefit their interests rather than those of other shareholders and the overall company. Furthermore, high ownership stakes among management may result in a preference for maintaining the status quo and avoiding risks, rather than pursuing innovative changes that could potentially enhance firm performance. This behavior may be attributed to management's focus on safeguarding their positions and authority within the company, rather than actively striving for optimal company development. This finding is different from the research conducted by Khan et al. (2020), Alabdullah (2018), Dakhlallh et al. (2021), and Hossain et al. (2021), but is consistent with the findings of Silviana & Widoatmodjo (2021). Hence, the first hypothesis of this study is rejected.

Hypothesis Testing (H_2)

The influence of IO on firm performance was found to be statistically insignificant. This statement is supported by the analysis results, which show a probability value of 0.9945, exceeding the research significance level of 0.05, indicating that the impact of IO on firm performance is not statistically significant. This could be explained by the fact that institutional investors, who tend to hold significant shares, often adopt long-term investment approaches and are not actively involved in the daily operational decisions of the company. Institutional shareholders tend to select companies with good financial performance, so the company's performance may already be favorable before the institution acquires shares. These findings are not consistent with the research conducted by Setiawan and Syarif (2019), Khorunnisa and Karina (2021), Novilia and Rasyid (2022), and Anggara and Muid (2021), but are consistent with the findings of Nugroho & Widiasmara (2019).

Hypothesis Testing (H_3)

The findings of the hypothesis test indicate that GO does not significantly impact firm performance, resulting in the hypothesis being dismissed. This is because the government's motivations and interests go beyond mere financial gains from owning company shares, including considerations such as maintaining employment and political positioning. Additionally, government intervention in company operations can hinder efficiency and flexibility, as well as dampen management's drive for innovation and improve firm performance. These results contradict the findings of Dianitasari and Hersugondo (2020), Hunardy and Tarigan (2017), and Sihombing and Akbar (2022), but align with the studies undertaken by Angela et al. (2019) and Ishak et al. (2022) that GO has no significant influence on firm performance.

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Hypothesis Testing (H_4)

The outcomes of the hypothesis testing for the fourth hypothesis reveal that FO does not have a statistically significant influence on firm performance. Thus, the fourth hypothesis of this study is declined. This can be attributed to the passive involvement of foreign shareholders in operational decision-making and their focus on long-term financial performance rather than short-term company performance. Additionally, foreign shareholders are constrained by local regulations, limiting their intervention in company operations. These findings are consistent with prior studies by Indarwati et al., (2015), Anisah and Hartono (2022), and Ivan and Raharja (2021), but contradict the findings of Dewi et al., (2020).

Hypothesis Testing (H_5)

DAR was unable to significantly impact ROE as a measure of firm performance, resulting in non-significant findings. This condition arises because ROE reflects the net income attributable to shareholders from invested capital, while DAR measures the level of debt compared to assets. Given this situation, DAR may not fully influence ROE, leading to non-significant results. These findings are consistent with Agustina and Santosa (2019) and Dana et al., (2021), but contradict the studies conducted by Krisyadi and Rionaldo (2021), Rahman (2020), and Wahyuni (2022), which found a substantial positive impact.

Hypothesis Testing (H_6)

The use of ROA as a measure of company performance is not affected by the DER. This scenario indicates that the company does not heavily rely on debt as the primary source of funding for its operations. Consequently, the amount of debt does not significantly impact the profitability of the company. This finding aligns with the study conducted by Dana et al., (2021). In contrast, the firm's performance measured by ROE can be negatively influenced by DER. A substantial ROE suggests that the company is effectively generating profits, and when the company has a high debt ratio, it has to use net income to pay interest expenses. This condition affects the capital invested by the company's owners and hurts ROE. Therefore, companies with a low DER tend to create higher ROE, due to lower financial burdens, and vice versa. This study contradicts the research conducted by Hidayat et al. (2022), and Wiranawata (2022), but is aligned with the study by Lestari (2020).

CONCLUSION

The outcomes of this study shed light on the intricate dynamics of ownership structure's influence on firm performance. The comprehensive framework, encompassing managerial, institutional, government, and foreign ownership, emerges as a complex determinant that does not significantly affect firm performance. This conclusion is drawn from a careful analysis of ROA and ROE. However, delving deeper into the details, it becomes evident that DAR exerts a noteworthy and adverse impact on ROA, while intriguingly leaving ROE unaffected. On a different note, the impact of DER plays out in a nuanced manner. While no noticeable effect on ROA is seen, it has the potential to negatively affect ROE. Furthermore, the meticulous consideration of firm size as a control variable unveils a statistically significant positive correlation with firm performance. These results emphasize the potential influence of ownership structure and capital structure on the overall performance of the firm, while also underscoring the importance of considering other factors such as risk management, financial policies, and economic conditions in the analysis of firm performance.

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