

## Analysis of Market Capitalization and Fundamental Factors on Firm Value

**Irma Sari Permata<sup>1\*</sup>, Fatima Tuzzahara Alkaf<sup>2</sup>**

<sup>1),2)</sup> Faculty of Economic and Business Universitas Pancasila, Indonesia, email:

[sari.permata11@univpancasila.ac.id](mailto:sari.permata11@univpancasila.ac.id)

\*Corresponding Author: Irma Sari Permata<sup>1</sup>

**Abstract:** The purpose of this study is to analyze the effect of market capitalization and fundamental factors on the value of manufacturing companies listed on the Indonesia Stock Exchange from 2014 to 2018. The variables utilized in this study are market capitalization, variables of micro-company such as company size, free cash flow, dividend policy (DPR), and macro variables, namely interest rates to the value of the company (Tobin'Q). Therefore it can be to assess the development of good company conditions. The method of this research is explanatory research and samples were taken by purposive sampling from a population of manufacturing companies that satisfy the sample criteria. Furthermore, the analysis of this research conducted multiple linear regression analysis.

**Keywords:** Market Capitalization, Fundamental Factors, Company Value

### INTRODUCTION

Firm value is an important concept for investors, because it is considered an indicator for the market to assess the company as a whole. High firm value causes the level of investor confidence in the company is also higher. That is because investors' assessment of the company's good prospects in the future is be observed in its high share price.

The success of a company is often associated with stock prices. The company can provide maximum prosperity to shareholders if the share price increases. The higher the share price of a company, the higher the prosperity of its shareholders.

The rise and fall of stock prices in the capital market is an interesting phenomenon to be discussed at this time. The global economic crisis that occurred in 2008 produced a significant impact on the capital market in Indonesia, which was reflected in a fall in share prices of up to 40-60 percent from its initial position in 2008 (Kompas, 2008). This phenomenon is caused by the action of releasing shares by foreign investors who need liquidity and is exacerbated by the subsequent domestic investors who also release shares in a rollicking. The condition is considered to affect the value of the company because the value of the company is reflected in its share price.

All sample companies experienced fluctuations in the value of companies that went up and down. Especially in 2008, all company values experienced a decline. This is interesting to study, what caused fluctuations in the rise and fall of companies in Indonesia after the crisis period. Companies that experience a decline in firm value should immediately make improvements, thus not to reduce the company's credibility in the eyes of investors.

Companies that have “go public” can see the value of their firm from the value of shares in the capital market. Share value is defined by the number of shares multiplied by the market value per share plus the value of debt. By assuming that if the debt value is constant, then directly increasing the value of the stock will increase the value of the company. Some use measurements with Tobin's Q dimensions. This ratio is the ratio that can provide the best information in reflecting the value of the company because in its calculation, this ratio involves all elements of the company's debt and capital stock, which includes not only ordinary shares and shareholders' equity, but all assets owned by the company.

Stock as one of the securities instruments that are traded on the capital market, the price will always fluctuate up and down. This is certainly a consideration for potential investors if they are going to buy shares in the capital market first to conduct an analysis before investing. The analysis that can be done by potential investors is stock analysis, where there are two basic assessments namely technical analysis and fundamental analysis. Technical analysis is a security analysis technique that combines historical data on stock price developments and trade volume. While fundamental analysis is one method of stock selection to assess whether or not a company's stock is good or not. Basically, fundamental analysis is an analysis of fundamental factors that will affect the value of a company's stock, with a focal point on macroeconomic conditions, industrial conditions and micro-conditions of the company.

This research assumes that investors use fundamental aspects as a basis for valuing stock investments. Fundamental factors are not only in the microcomputer that can be controlled by the company, but also macros that are outside the company's control, such as inflation, interest rates and exchange rates. The economic crisis marked by rising inflation, interest rates and exchange rates will affect the behavior of investors in making investment decisions on the capital market. This is a challenge and a difficult task for managers to keep the company in existence through policies that can maintain the fundamental conditions and market prices of the company's stock in the capital market.

To be able to get a picture of a company's financial development, it is necessary to conduct an analysis or interpretation of financial data from the company concerned, where the financial data is reflected in the financial statements. The research sample of 11 manufacturing companies listed on the Indonesia Stock Exchange during the period 2014 to 2018 based on certain criteria.

Research on micro fundamental factors by processing data sourced from internal companies, especially financial statements issued officially by the company so that it can be known about the value of the company has been done and among these studies show different results.

## **LITERATURE REVIEW**

Value of the firm is a certain condition that has been achieved by a company as an illustration of public trust in the company after going through a process of activities for several years, ie since the company was founded until now. Increasing the value of the company is an achievement, in accordance with the wishes of the owners, because with the increase in the value of the company, the welfare of the owners will also increase.

Value of the firm is very important because it reflects the company's performance which can affect investors' perceptions of the company. High company value will make the

market believe about the current state of the company or the prospects of the company in the future of the company or the prospects of the company in the future (Wijaya & Sedana, 2015). For companies that issue shares in the capital market, the price of shares traded on the stock exchange is an indicator of company value. The higher the stock price of a company the higher the value of the company which has an impact on the greater prosperity of the owner of the company. The higher the stock price of a company the higher the value of the company which has an impact on the prosperity of the owner of the company. Company value can be measured using Tobin'Q.

The main indicators of company value can be measured from various points of view. This means that the value of the company is said to be good when viewed from a certain perspective. Company value can be seen from market capitalization, company size, free cash flow, dividend policy, interest rates. Based on this the researcher wants to know the effect of market capitalization, company size, free cash flow, dividend policy, interest rates on firm value.

### ***Market Capitalization and Firm Value***

Investors who invest in the Indonesia Stock Exchange (IDX), in addition to taking into account the fundamental conditions and business prospects of one issuer, also take into account the development of the capitalization value of the relevant shares. The capitalization value per individual share determines the market capitalization value of one stock. Thus, the market capitalization value is an illustration of the market value of one company while also reflecting the market value of one stock market.

An investor is advised to look at the value of the stock market capitalization that will be used as an investment. Stocks with small market capitalization indicate a small size of the company in terms of assets and capital. This is that the company has a high growth potential and will ultimately provide a high return in the future that will come when investing in these shares. Although it provides a high potential return, companies with small market capitalization have more business risk and higher uncertainty. Conversely, stocks, with large market capitalization, indicate that the company is already in a mature business cycle, so the potential to grow again is very small. Based on the explanation, the hypothesis proposed is:

H<sub>1</sub>: Market Capitalization has a significant effect on firm value

### ***Company Size and Firm Value***

Company size is an indicator that shows the company's financial strength. The greater the assets of a company, the greater the capital invested, the greater the total sales of a company, the more money turnover and the greater the market capitalization, the greater the company is known to the public.

The size of the company is measured by the total assets of the company obtained by the company's financial statements. The size of the company is considered able to influence the value of the company. The large size of the company reflects that the company is experiencing good growth and growth thereby increasing the value of a company. The empirical study by (Oktaviani, Rosmaniar, & Hadi, 2019) found that company size had a significant effect on firm value. The statement was also supported by researchers such as (Fadhil, 2015), (Armadi, 2016) and (Dang, Vu, Ngo, & Hoang, 2019), who stated that company size had a significant positive effect on firm value. Based on these explanations, the proposed hypothesis is:

H<sub>2</sub>: Company size has a significant effect on firm value

### ***Free Cash Flow and Firm Value***

Free cash flow is a fund owned by a company outside of funds for working capital intended for distribution to creditors and shareholders. According to the signaling theory,

high profitability is a positive signal, plus the company has a high free cash flow so that it will increase investor confidence that the company is able to provide high returns in the form of dividends, (Brigham & Houston, 2009). The high free cash flow owned by the company will show that the company is healthier, because the company has free cash available, indicating that the company is in good condition. Research conducted by (Al Zararee & Al-Azzawi, 2014) and (Dewi, Sari, Budiasih, & Suprasto, 2019) shows that free cash flow has a positive significant effect on firm value. The hypothesis proposed in this study is:

H<sub>3</sub>: Free cash flow has a significant effect on firm value

#### ***Dividend Policy and Firm Value***

Another determinant factor that affects a company's value is dividend policy. The high dividend shows a good company performance that will increase investor attractiveness. Dividend signal theory explains that the company's future can be seen from the level of dividends paid (Van Horne & Wachowicz, 2009). The higher the level of dividend payments will also increase the information content of the dividend itself and the value of the company so that it will increase market confidence (Sudana, 2011). Research (Farrukh, Irshad, Khakwani, Ishaque, & Ansari, 2017) and (Nwamaka & Ezeabasili, 2017) states that dividend policy has a significant positive effect on firm value. The hypothesis proposed in this study is:

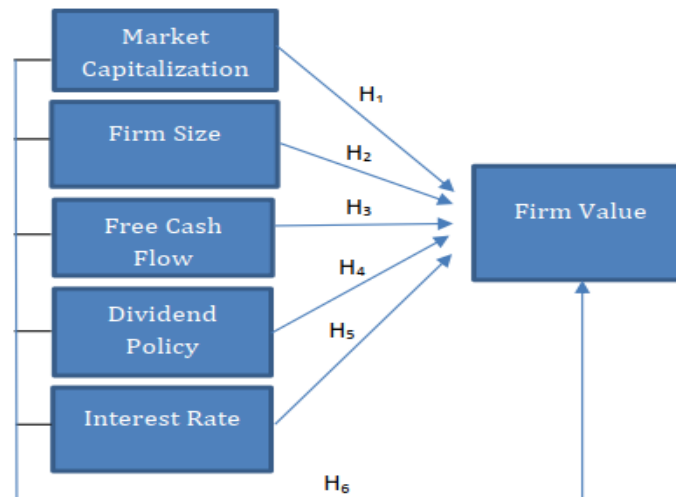
H<sub>4</sub>: Dividend policy has a significant positive effect on firm value

#### ***Interest Rates and Firm Value***

Rising interest rates will encourage people to save, and lazy to invest in the real sector. An increase in the interest rate will also be borne by investors, in the form of an increase in interest costs for the company. The public does not want to risk investing in high costs, as a result the investment becomes undeveloped. Many companies have difficulty maintaining their lives, and this causes the company's performance to decline. The decline in company performance can result in a decrease in stock prices, which means the value of the company will also decline. The empirical study by Afriyani (2018) and Ebenezer et. al. (2019) states that interest rates have a significant effect on firm value. The hypothesis proposed in this study is:

H<sub>5</sub>: Interest rates have a significant effect on firm value

Based on the basic of theoretical and empirical study of firm value, market capitalization, company size, free cash flow, dividend policy, interest rates and also studies of previous studies, the following is presented empirical research models to determine the effect of market capitalization, company size, free cash flow, dividend policy, interest rates either partially or simultaneously on the company's value. So the empirical research model can be described as follows:



**Figure 1. Research Framework**

## RESEARCH METHODOLOGY

### *Research Design*

The design of this research is a literature study and the type of research conducted is explanatory research, namely research that aims to test a theory or hypothesis in order to strengthen or even reject a theory or hypothesis of existing research results. This explanatory research is fundamental and aims to obtain information, data information about things that are not yet known. The results of this study are expected to provide an accurate explanation related to the research objectives to be achieved.

### *Population and Sampling Procedure*

The population in this study are manufacturing companies that have been listed on the Indonesia Stock Exchange (BEI) for 5 periods, from 2014 to 2018 and the determination of the sample conducted purposive sampling.

### *Operationalization of Variables*

This study uses three (3) independent or independent variables, namely liquidity, solvency and dividend policy, and one (1) dependent variable, which is the firm's value variable.

**Table 1. Operationalization Variables**

Variables	Proxy
Firm Value (Y)	Tobin'Q
Market Capitalization (X1)	$V_s = P_s \times S_s$
Firm Size (X2)	UKUR (log to totalassets)
Free Cash Flow (X3)	RETA ( <i>Retained Earning to Asset</i> )
Dividend Policy (X4)	DPR
Interest Rate (X5)	Nominal interest rate = real interest rate + inflation

### *Analysis Techniques*

The analysis technique used in this study is multiple linear regression. The reason for choosing multiple linear regression models is to test the effect of several independent variables on the dependent variable. The regression model used in this study is multiple linear regression with the following equation:

$$Y = a + b_1X_1 + b_2X_2 + b_3X_3 + b_4X_4 + b_5X_5 + e$$

Y : Firm Value

a : Constanta

b : Coefficient of regression direction

X1: Market Capitalization

X2: Firm Size

X3: Free Cash Flow

X4: Dividend Policy

X5: Interest Rate

e : Error term

## RESULTS AND DISCUSSION

The initial stage of multiple linear regression testing is testing the classical assumptions which consist of tests of normality, multicollinearity, heterocedasticity, and autocorrelation. The empirical data used in this study shows that the research model has fulfilled all assumptions so that the interpretation of the regression equation can be done. Hypothesis test

To test the significance of the simultaneous effect of independent variables (X) on the dependent variable (Y), the F test is carried out. To partially test the effect of the independent variables (X) on the dependent variable (Y), then t test was performed. While multiple regression analysis is used to determine whether there is influence between three independent variables (X), namely Market Capitalization (X1), Company Size (X2), Free Cash Flow (X3), Dividend Policy (X4) and Interest Rate (X5) with variables not free (Y), that is company value.

**Table 2. Regression Results**

Variables	Coefficients	T test	Sig	VIF
Constanta	-3,097	-0,812	0,421	–
Market Capitalization	0,956	6,099	0,000	4,238
Company Size	- 0,766	- 3,133	0,003	6,172
Free cash Flow	-1,594	- 2,354	0,023	2,079
Dividend Policy	- 0,003	- 0,426	0,672	1,181
Interest Rate	0,037	0,458	0,649	1,046
Normality Test				
F test	0,000			
Adjusted R <sup>2</sup>	0,492			
DW value	0,948			

a. Dependent Variable: TOBINS'Q

The significance value generated in the F test is 0,000. Because  $0,000 < 0,050$ , Ho's decision was rejected. From these tests it was concluded that Market Capitalization (X1), Company Size (X2), Free Cash Flow (X3), Dividend Policy (X4) and Interest Rate (X5) simultaneously had a significant effect on Company Value (Y).

While the partial test resulted in variable X significantly influence the variable Firm Value (Y), namely the Market Capitalization variable (X1) with a p-value of  $0,000 < 0,050$ , Company Size (X2) with a p-value of  $0,003 < 0,050$ , Free Cash Flow (X3) with a p-value of  $0,023 < 0,050$ . While the Dividend Policy variable (X4) with a p-value of  $0,672 > 0,050$  and the Interest Rate (X5) with a p-value of  $0,649 > 0,050$  has no significant effect on firm value. The multiple regression equation model in this study is:

$$Y = - 3,097 + 0,956X1 - 0,766X2 - 1,594X3 - 0,003X4 + 0,037X5 + e$$

If Market Capitalization (X1), Company Size (X2), Free Cash Flow (X3), Dividend Policy (X4) and Interest Rate (X5) are considered constant or zero, then the value of the



company is -3,097. Every increase of Market Capitalization (X1) by one unit will increase the value of the company by 0.956 units. Each increase in Company Size (X2) by one unit will reduce the value of the company by 0.766 units. Each increase in Free Cash Flow (X3) by one unit will reduce the value of the company by 1,594 units. Each increase in Dividend Policy (X4) by one unit will reduce the value of the company by 0.003 units. And each increase in the Interest Rate (X5) of one unit will increase the value of the company by 0.037 units.

The adjusted R<sup>2</sup> result of 0.492 means that the company's value variable is influenced by the variable Market Capitalization (X1), Company Size (X2), Free Cash Flow (X3), Dividend Policy (X4) and Interest Rate (X5) by 49.2% while the rest is equal to 50.8% is influenced by other independent variables outside the research model.

Market Capitalization (X1) has been proven to have a significant effect on firm value with a coefficient of 0.956 (sig 0,000 < 0.050). This positive coefficient value indicates that the greater the market capitalization, it will increase the value of the company. The results of this study support the findings of (Ayu S & Ayu D, 2016), (Susilawati, 2014), and (Nurhayati, 2013).

Company size (X2) has been proven to have a negative significant effect on firm value with a coefficient of - 0.766 (sig 0,000 < 0.050). This finding is accordance with the findings of (Susanti & Restiana, 2018) and (Hirdinis, 2019).

Free Cash Flow (X3) is proven to have a negative significant effect on company value with a coefficient of - 1.594 (sig 0.023 < 0.050). The outcomes of this research support the findings of (Profita & Ratnaningsih, 2016) and (Wahyuddin & Salsabila, 2019).

Dividend policy (X4) has not been proven to have a significant effect on firm value with a coefficient - 0.003 (sig 0.672 > 0.050), thus H4 is not supported. This negative coefficient value indicates that the greater the dividend policy provided by the company, the smaller the increase in the value of the company. The results of this study support the findings of (Anggeriani, Fachrudin, & Silalahi, 2018) (Esana & Ari, 2017), and (Senata, 2016). Information asymmetry between investors and company managers has an impact on investor responses related to company dividend policies which then affect the value of the company. This can be interpreted that investors interpret changes in the dividend rate in management's view as the prospect of future profits for the company.

Interest Rate (X5) has not been proven to have a significant effect on firm value with a coefficient of 0.037 (sig 0.649 > 0.050), thus H5 is not supported. The results of this study support the finding by (Ayturk, Gurbuz, & Yanik, 2016) and (Frensidya & Mardhaniatya, 2019).

## CONCLUSION

The results of this study are variable market capitalization, company size and free cash flow, which supports the hypothesis that market capitalization, company size and free cash flow have a significant effect on firm value. While dividend policy and interest rates do not significantly influence the value of the company. The company determines the amount of dividends distributed to investors, the reduction in the amount of dividends paid is often a signal to investors regarding the company's future growth prospects. Indirectly investors can estimate the value of the company to be invested in capital.

## REFERENCES

- Afriyani. (2018). Influence of Micro Fundamental Factors and Macroeconomics on Stock Return and Manufacturing Value of Companies Listed in Indonesia Stock Exchange (IDX). *Quest Journals: Journal of Research in Humanities and Social Science*, Volume 6, Issue 5, 49-57.

- Al Zararee, A. N., & Al-Azzawi, A. (2014). The Impact of Free Cash Flow on Market Value of Firm. , *Global Review of Accounting and Finance*, Volume 5, No. 2., 56- 63.
- Anggeriani, Fachrudin, K. A., & Silalahi, A. S. (2018). The Effect Of Dividend Policy, Firm Size and Capital Structure On Firm Value with Corporate Social Responsibility As A Moderation Variable In Open Mining Companies In Indonesia Stock Exchange. *IOSR Journal of Business and Management (IOSR- JBM)*, Volume 20, Issue 11, 70-82.
- Armadi, I. W. (2016). Pengaruh Profitabilitas, Leverage, dan Ukuran Perusahaan Pada Nilai Perusahaan Melalui Pengungkapan Tanggung Jawab Sosial. *E-Jurnal Akuntansi Universitas Udayana*, Volume 17 No.1 , 233-256.
- Ayturk, Y., Gurbuz, A. O., & Yanik, S. (2016). Corporate derivatives use and firm value: Evidence from Turkey. *Borsa Istanbul Review* Volume 16, Issue 2, 108-120.
- Ayu S, N. K., & Ayu D, N. P. (2016). Pengaruh Profitabilitas, Likuiditas, Pertumbuhan, dan Investment Opportunity Set terhadap Nilai Perusahaan. *E-Jurnal Manajemen Unud*. Volume 5 No.7.
- Brigham, E. F., & Houston, J. F. (2009). *Dasar-dasar Manajemen Keuangan*, Buku Satu, Edisi Kesepuluh, Alih Bahasa Ali Akbar Yulianto. . Jakarta: Salemba Empat.
- Dang, H. N., Vu, V. T., Ngo, X. T., & Hoang, H. T. (2019). Study the Impact of Growth, Firm Size, Capital Structure, and Profitability on Enterprise Value: Evidence of Enterprises in Vietnam. *The Journal of Corporate Accounting & Finance* Volume 30 Issue 1, 144-160.
- Dewi, I. A., Sari, M. M., Budiasih, I., & Suprasto, H. B. (2019). Free Cash Flow Effect Towards Firm Value. *International Research Journal of Management, IT & Social Sciences*, Volume 6 No. 3.
- Ebenezer, O. O., Islam, M. A., Yusoff, W. S., & Rahman, S. (2019). The Effects of Liquidity Risk and Interest-Rate Risk on Profitability and Firm Value among Banks in ASEAN-5 Countries. *Journal of Reviews on Global Economics*, Volume 8, 337-349.
- Esana, R., & Ari. (2017). Pengaruh Kebijakan Dividen dan Keputusan Investasi terhadap Nilai Perusahaan serta dampaknya terhadap Profitabilitas t+1. *Jurnal Administrasi Bisnis (JAB)*.Volume 50. No.6.
- Fadhil, M. (2015). Pengaruh Likuiditas, Solvabilitas dan Profitabilitas terhadap Nilai Perusahaan dengan Kebijakan Dividen sebagai Variabel Moderasi pada Perusahaan Perbankan, Asuransi & Lembaga Keuangan Lainnya di Bursa Efek Indonesia Tahun 2010 – 2013. *Jom FEKON* Volume 2 No. 2.
- Farrukh, K., Irshad, S., Khakwani, M. S., Ishaque, S., & Ansari, N. Y. (2017). Impact of dividend policy on shareholders wealth and firm performance in Pakistan. *Taylor & Francis Online: Journal Cogent Business & Management*, Volume 4, Issue 1.
- Frensidya, B., & Mardhaniatya, T. I. (2019). The Effect of Hedging with Financial Derivatives on Firm Value at Indonesia Stock Exchange. *LPEM FEB UI: Economics and Finance in Indonesia* Volume 65 No. 1, 20-32.
- Hirdinis, M. (2019). Capital Structure and Firm Size on Firm Value Moderated by Profitability. *International Journal of Economics and Business Administration* Volume 7, Issue 1, 174-191.
- Kompas. (2008). *Ketika Krisis dan Bursa Global Berjatuh?* Jakarta: Kompas.
- Nurhayati. (2013). Profitabilitas, Likuiditas dan Ukuran Perusahaan Pengaruhnya terhadap Kebijakan Dividen dan Nilai Perusahaan Sektor Non Jasa. *Jurnal Keuangan dan Bisnis*, 67-98.
- Nwamaka, O. C., & Ezeabasili. (2017). Effect of Dividend Policies on Firm Value: Evidence from quoted firms in Nigeria. *International Journal of Management Excellence* Volume 8 No.2.



- Oktaviani, M., Rosmaniar, A., & Hadi, S. (2019). Pengaruh Ukuran Perusahaan (Size) Dan Struktur Modal Terhadap Nilai Perusahaan. *BALANCE: Economic, Business, Management and Accounting Journal*, Volume 16, No. 1.
- Profita, A. S., & Ratnaningsih, D. (2016). The Impact Of Free Cash Flow On The Firm Value. *Journal of Economy Accountancy International* , 1-12.
- Senata, M. (2016). Pengaruh Kebijakan Dividen erhadap Nilai Perusahaan yang tercatat pada Indeks LQ-45 Bursa Efek Indonesia. . *Jurnal Wira Ekonomi Mikroskil*. Volume 6 No. 01.
- Sudana, M. I. (2011). *Manajemen Keuangan Perusahaan*. Jakarta: Erlangga.
- Susanti, N., & Restiana, N. G. (2018). What's the Best Factor to Determining Firm Value? *Journal of Finance and Banking* Volume 22, No. 2.
- Susilawati. (2014). Pengaruh Kebijakan Dividen, Keputusan Investasi, Keputusan Pendanaan, Kepemilikan Institusional dan Likuiditas terhadap Nilai Perusahaan pada Perusahaan Manufaktur yang terdaftar di Bursa Efek Indonesia Periode 2010-2013. *Jurnal Akuntansi* , 40-65.
- Van Horne, J., & Wachowicz, J. (2009). *Prinsip-prinsip Manajemen Keuangan*. Jakarta: Salemba Empat.
- Wahyuddin, A., & Salsabila, K. (2019). Firm Size Moderates the Effect of Free Cash Flow, Firm Growth, and Profitability on Debt Policy. *Jurnal Dinamika Akuntansi*, Volume 11, No. 1, p-ISSN 2085-4277 | e-ISSN 2502-6224 , 89-97.
- Wijaya, B. I., & Sedana, I. B. (2015). Pengaruh Profitabilitas Terhadap Nilai Perusahaan (Kebijakan Dividen Dan Kesempatan Investasi Sebagai Variabel Mediasi). *E- Jurnal Manajemen*, Volume 4, No.12.