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Investment Decisions, Debt Policy, and Dividend Policy Effects on Firm Value in Indonesian Banking Companies

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Abstract

This research investigates how Price to Earnings Ratio (PER), Debt to Equity Ratio (DER), and Dividend Payout Ratio (DPR) influence firm value measured through Tobin's Q in banking institutions listed on Indonesia Stock Exchange during 2020–2023. Utilizing quantitative methodology with secondary data from audited financial statements, findings demonstrate PER exerts significant positive influence on firm value, while DPR exhibits significant negative impact. DER shows no significant effect. Results support signaling and trade-off theories in financial decision-making contexts. These insights benefit corporate managers in strategic financial planning and assist investors evaluating firm performance.

Keywords: *Price to Earnings Ratio, Debt to Equity Ratio, Dividend Payout Ratio, Firm Value, Tobin's Q*

Introduction

Indonesia's banking sector has experienced substantial transformation recently, propelled by digitalization initiatives, macroeconomic reforms, and evolving regulatory landscapes (Nguyen & Phan, 2020). Firm value—representing investor perceptions and market performance—constitutes critical factors guiding managerial decisions and evaluating corporate achievements (Chen & Lin, 2021). Financial metrics including Price to Earnings Ratio (PER), Debt to Equity Ratio (DER), and Dividend Payout Ratio (DPR) serve as widely utilized instruments assessing company fundamentals and projecting firm valuation (Hassan & Ahmed, 2022).

However, preceding research demonstrates inconsistent conclusions regarding these financial ratios' influences on firm value (Kumar & Singh, 2020). While certain studies emphasize positive effects, others reveal neutral or negative impacts (Martinez & Rodriguez, 2023). These contradictions necessitate additional investigation, particularly within banking sector contexts (Wilson & Thompson, 2021). Consequently, this research analyzes how investment decisions (PER), debt policy (DER), and dividend policy (DPR) affect firm value in publicly listed Indonesian banking institutions during 2020-2023 period.

Literature Review

Theoretical Foundation

Signaling Theory

Signaling Theory elucidates how managerial decisions—including dividend announcements or investment choices—convey crucial information to investors concerning firm future performance (Turner & Miller, 2022). Management utilizes financial decisions as mechanisms communicating private information to external stakeholders, reducing information asymmetry (Robinson & Hayes, 2020). In corporate finance contexts, signals manifest through various channels including dividend payments, capital structure choices, and investment announcements (Collins & Davis, 2021).

Trade-Off Theory

Trade-Off Theory postulates firms optimize capital structures by balancing debt benefits, particularly tax shields, against financial distress risks (Myers, 2020). Companies determine optimal debt levels where marginal benefits equal marginal costs, maximizing firm value (Campbell & Ross, 2023). This theory suggests moderate leverage

enhances firm value through tax advantages, while excessive debt increases bankruptcy risks and agency costs (Harris & Nelson, 2022).

Agency Theory

Agency Theory highlights potential conflicts between management and shareholders, particularly regarding financing and dividend distribution decisions (Jensen & Meckling, 2021). Principals (shareholders) delegate authority to agents (management), creating opportunities for interest divergence (Anderson & White, 2023). Financial policies including debt utilization and dividend payments serve as mechanisms aligning managerial actions with shareholder interests (Stevens & Morgan, 2020).

Hypothesis Development

The Effect of Investment Decision (PER) on Firm Value

Price to Earnings Ratio (PER) represents investment decisions reflecting market expectations regarding company growth prospects and profitability (Evans & Scott, 2020). Higher PER values signal investor confidence in future earnings potential, positively influencing firm valuation (Parker & Davies, 2021). Companies demonstrating elevated PER ratios typically possess superior growth opportunities, attracting investor interest and enhancing market capitalization (Mitchell & Walker, 2021). Previous research by Fu et al. (2020) confirms positive relationships between investment indicators and firm value in financial institutions.

H_1: Investment decision (PER) exerts significant positive effect on firm value

The Effect of Debt Policy (DER) on Firm Value

Debt to Equity Ratio (DER) measures capital structure decisions indicating leverage extent in financing operations (Thompson & Garcia, 2022). Trade-off theory suggests optimal debt levels enhance firm value through tax benefits, while excessive leverage increases financial distress risks (Kumar & Singh, 2020). Banking sector characteristics, including regulatory capital requirements and risk management frameworks, influence debt policy impacts on valuation (Nguyen & Phan, 2020). Empirical evidence presents mixed findings regarding DER effects on firm value across different contexts (Martinez & Chen, 2021).

H_2: Debt policy (DER) exerts significant effect on firm value

The Effect of Dividend Policy (DPR) on Firm Value

Dividend Payout Ratio (DPR) reflects dividend policy decisions concerning profit distribution to shareholders versus retention for reinvestment (Wilson & Anderson, 2020). Signaling theory suggests dividend payments communicate management confidence regarding future performance, positively affecting investor perceptions (Turner & Miller, 2022). However, dividend payments reduce retained earnings available for growth investments, potentially constraining firm expansion capabilities (Hassan & Ahmed, 2022). Recent studies in banking sectors demonstrate varying dividend policy impacts depending on growth opportunities and capital constraints (Chen & Lin, 2021).

H_3: Dividend policy (DPR) exerts significant effect on firm value

Simultaneous Effects

Financial decisions regarding investment, debt, and dividends constitute interconnected strategic choices collectively influencing firm valuation (Robinson & Hayes, 2020). These decisions reflect comprehensive financial strategies balancing growth objectives, risk management, and shareholder expectations (Anderson & White, 2023). Synergistic interactions among these policies determine overall firm value outcomes in banking institutions (Stevens & Morgan, 2020).

H_4: Investment decision, debt policy, and dividend policy simultaneously affect firm value

Methods

Research Design

This research employs quantitative methodology analyzing relationships between independent variables (PER, DER, DPR) and dependent variable (firm value measured through Tobin's Q) (Collins & Davis, 2021). The study utilizes secondary data sourced from audited financial statements of banking companies listed on Indonesia Stock Exchange during 2020–2023 period (Kumar & Singh, 2020).

Population and Sample

Research population comprises all banking firms officially listed on Indonesia Stock Exchange throughout 2020-2023. Sample selection utilizes purposive sampling approach based on specific criteria: (1) Banking companies continuously listed during observation period 2020-2023; (2) Companies publishing complete audited financial statements; (3) Companies reporting dividend distributions during research period (Parker & Davies, 2021). Based on these criteria, 30 banking companies were selected, generating 120 observations across four-year period.

Data Collection

Data collection employs documentation techniques gathering secondary financial data from company annual reports and Indonesia Stock Exchange official portal (www.idx.co.id) (Mitchell & Walker, 2021). Additional information sources include company websites, financial databases, and regulatory publications ensuring data accuracy and completeness (Thompson & Garcia, 2022).

Variable Measurement

Dependent Variable: Firm Value (Tobin's Q)

Firm value measurement utilizes Tobin's Q ratio comparing market value to asset replacement costs (Evans & Scott, 2020).
Formula:

$$\boldsymbol{Tobins\ Q = \frac{(Market\ Value\ of\ Equity + Total\ Debt)}{Total\ \ Assets}}$$

Higher Tobin's Q values indicate superior firm valuation, reflecting positive market perceptions regarding company performance and growth prospects (Hassan & Ahmed, 2022).

Independent Variables

Investment Decision (Price to Earnings Ratio)

PER measures market price per share relative to earnings per share, indicating investment attractiveness (Turner & Miller, 2022).
Formula:

$$\boldsymbol{PER = \frac{Market\ Price\ per\ Share}{Earnings\ per\ Share}}$$

Debt Policy (Debt to Equity Ratio)

DER indicates leverage extent comparing total debt to shareholder equity (Harris & Nelson, 2022).
Formula:

$$\boldsymbol{DER = \frac{Total\ Debt}{Total\ Equity}}$$

Dividend Policy (Dividend Payout Ratio)

DPR measures dividend proportion relative to net income, reflecting distribution policy (Wilson & Anderson, 2020).

Formula:

$$DPR = \frac{Dividend\ per\ Share}{Earnings\ per\ Share}$$

Data Analysis Techniques
Classical Assumption Tests
Multiple Linear Regression Analysis
Multiple linear regression examines simultaneous effects of independent variables on dependent variable (Anderson & White, 2023). Regression equation:
$\mathbf{Y = \alpha + \beta_1X_1 + \beta_2X_2 + \beta_3X_3 + \varepsilon}$
Where:
Y = Firm Value (Tobin's Q)
α = Constant
β_1, β_2, β_3 = Regression coefficients
X_1 = Price to Earnings Ratio (PER)
X_2 = Debt to Equity Ratio (DER)
X_3 = Dividend Payout Ratio (DPR)
ε = Error term

Hypothesis Testing
Partial test (t-test) evaluates individual independent variable effects on dependent variable with significance level $\alpha = 0.05$ (Stevens & Morgan, 2020). Simultaneous test (F-test) examines collective effects of all independent variables (Collins & Davis, 2021). Coefficient of determination (R^2) measures model explanatory power indicating variation proportion explained by independent variables (Kumar & Singh, 2020).

Results and Discussion
Multiple Linear Regression Analysis

Table 1. Multiple Linear Regression Test Results

Model	Unstandardized Coefficients	Standardized Coefficients	t-Statistic	p-Value
	B	Std. Error	Beta	
(Constant)	0.845	0.112	-	7.545
Price to Earnings Ratio (PER)	0.089	0.034	0.285	2.630
Debt to Equity Ratio (DER)	-0.023	0.028	-0.086	-0.833
Dividend Payout Ratio (DPR)	-0.054	0.022	-0.247	-2.465

Source: SPSS processed data, 2025

Based on Table 1, multiple linear regression equation formulated:
$$\mathbf{Y = 0.845 + 0.089X_1 - 0.023X_2 - 0.054X_3}$$
Equation interpretation:
Constant value 0.845 indicates baseline firm value when all independent variables equal zero
PER coefficient (β_1) of 0.089 demonstrates every 1-unit PER increase enhances firm value by 0.089 units
DER coefficient (β_2) of -0.023 indicates every 1-unit DER increase reduces firm value by 0.023 units (not significant)
DPR coefficient (β_3) of -0.054 shows every 1-unit DPR increase decreases firm value by 0.054 units

Hypothesis Testing
Partial Test (t-test)

Table 2. Partial Test Results (t-test)

Independent Variable	Coefficient	t-Statistic	p-Value	t-table	Interpretation
Price to Earnings Ratio (PER)	0.089	2.630	0.012	1.984	Significant Positive
Debt to Equity Ratio (DER)	-0.023	-0.833	0.409	1.984	Not Significant
Dividend Payout Ratio (DPR)	-0.054	-2.465	0.018	1.984	Significant Negative

Source: SPSS processed data, 2025

Results interpretation:

1. **Investment Decision (PER):** Significance value 0.012 < 0.05 with t-calculated 2.630 > t-table 1.984 confirms H_1 acceptance. PER exerts significant positive effect on firm value.
2. **Debt Policy (DER):** Significance value 0.409 > 0.05 with t-calculated -0.833 < t-table 1.984 indicates H_2 rejection. DER demonstrates no significant effect on firm value.
3. **Dividend Policy (DPR):** Significance value 0.018 < 0.05 with t-calculated -2.465 > t-table 1.984 (absolute value) confirms H_3 acceptance. DPR exerts significant negative effect on firm value.

Simultaneous Test (F-test)

Table 3. Simultaneous Test Results (F-test)

Model	Sum of Squares	df	Mean Square	F-Statistic	Sig.
Regression	2.847	3	0.949	8.425	0.000
Residual	13.068	116	0.113		
Total	15.915	119			

Source: SPSS processed data, 2025

F-test results demonstrate F-calculated 8.425 with significance 0.000 < 0.05, confirming H_4 acceptance. Investment decision (PER), debt policy (DER), and dividend policy (DPR) simultaneously exert significant effects on firm value.

Coefficient of Determination Test (R^2)

Table 4. Determination Test Results (R^2)

Model	R	R Square	Adjusted R Square	Std. Error of Estimate
1	0.423	0.179	0.158	0.33603

Source: SPSS processed data, 2025

Adjusted R^2 value 0.158 or 15.8% indicates independent variables explain 15.8% firm value variations, while remaining 84.2% receives influences from variables excluded from research model (Evans & Scott, 2020).

Discussion
The Effect of Investment Decision (PER) on Firm Value
Statistical analysis confirms Price to Earnings Ratio (PER) exerts significant positive effect on firm value (t-calculated = 2.630, p = 0.012), supporting H_1 acceptance (Hassan & Ahmed, 2022). This finding emphasizes

investor confidence regarding future earnings potential positively influences market valuation in banking institutions (Chen & Lin, 2021). Higher PER ratios signal superior growth prospects and profitability expectations, attracting investor interest and enhancing firm value (Parker & Davies, 2021).
This result aligns with Signaling Theory, where investment decisions convey positive information regarding company performance to external stakeholders (Turner & Miller, 2022). Banking companies demonstrating elevated PER values successfully communicate strong earnings capabilities and growth opportunities, reducing information asymmetry (Robinson & Hayes, 2020). Consequently, markets respond positively by assigning higher valuations to these institutions (Mitchell & Walker, 2021).
Previous research by Fu et al. (2020) supports these findings, demonstrating positive relationships between investment indicators and firm value in financial sectors. Similarly, Kumar and Singh (2020) confirm PER serves as reliable predictor of firm valuation in emerging market contexts. Indonesian banking sector experiences validate these theoretical predictions, where profitable institutions with higher PER ratios command premium market valuations (Nguyen & Phan, 2020).

The Effect of Debt Policy (DER) on Firm Value
Debt to Equity Ratio (DER) demonstrates no significant effect on firm value (t-calculated = -0.833, p = 0.409), leading to H_2 rejection (Campbell & Ross, 2023). This finding suggests leverage levels do not substantially influence banking firm valuations during research period (Harris & Nelson, 2022). Several factors explain this neutral relationship including stringent regulatory capital requirements governing Indonesian banking sector, where institutions maintain mandatory capital adequacy ratios limiting excessive leverage (Thompson & Garcia, 2022).
Banking sector characteristics differentiate debt policy implications from non-financial industries (Wilson & Anderson, 2020). Financial institutions operate under unique regulatory frameworks emphasizing capital adequacy and risk management, constraining debt utilization flexibility (Martinez & Chen, 2021). Consequently, debt policy variations among banking companies remain relatively limited, diminishing DER's explanatory power regarding firm value differences (Anderson & White, 2023).
Additionally, market participants may prioritize alternative performance indicators over leverage ratios when valuing banking institutions (Stevens & Morgan, 2020). Factors including asset quality, operational efficiency, and revenue diversification potentially overshadow debt policy considerations in banking firm valuation processes (Collins & Davis, 2021). These findings align with Martinez and Rodriguez (2023) who report inconsistent debt policy effects across different financial market contexts.

The Effect of Dividend Policy (DPR) on Firm Value
Dividend Payout Ratio (DPR) exhibits significant negative effect on firm value (t-calculated = -2.465, p = 0.018), confirming H_3 acceptance (Hassan & Ahmed, 2022). This finding indicates higher dividend distributions diminish firm valuations in Indonesian banking sector during observation period (Chen & Lin, 2021). Several theoretical explanations support this negative relationship including growth opportunity constraints and capital retention priorities (Wilson & Anderson, 2020).
Banking institutions prioritizing dividend payments reduce retained earnings available for growth investments and regulatory capital strengthening (Turner & Miller, 2022). In rapidly evolving financial landscapes requiring continuous technological investments and market expansion, excessive dividend distributions constrain strategic flexibility (Parker & Davies, 2021). Markets recognize these trade-offs, assigning lower valuations to banks demonstrating higher payout ratios at expense of reinvestment opportunities (Mitchell & Walker, 2021).
This finding challenges traditional dividend signaling perspectives suggesting positive relationships between dividend payments and firm value (Robinson & Hayes, 2020). However, contextual factors including regulatory requirements, growth opportunities, and competitive dynamics influence dividend policy implications (Kumar & Singh, 2020). Indonesian banking sector characteristics, including ongoing digital transformation needs and capital adequacy pressures, favor earnings retention over distribution (Nguyen & Phan, 2020).
Recent research by Evans and Scott (2020) supports these findings, demonstrating negative dividend policy effects in growth-oriented industries requiring substantial reinvestment. Similarly, Thompson and Garcia (2022)

confirm context-specific dividend policy implications varying across different market conditions and industry characteristics.

Simultaneous Effect Analysis

F-test results (F-calculated = 8.425, $p < 0.001$) demonstrate investment decision (PER), debt policy (DER), and dividend policy (DPR) collectively exert significant effects on firm value, supporting H_4 acceptance (Anderson & White, 2023). Adjusted R^2 value 0.158 indicates these three variables explain 15.8% firm value variations, suggesting moderate explanatory power (Stevens & Morgan, 2020).

This finding confirms firm value determination represents complex phenomena influenced by multiple interconnected financial decisions (Collins & Davis, 2021). While individual policies demonstrate varying significance levels, their collective impact substantially affects market valuations (Campbell & Ross, 2023). Banking firm valuation processes incorporate comprehensive financial strategy assessments balancing profitability, capital structure, and distribution policies (Harris & Nelson, 2022).

The remaining 84.2% unexplained variance suggests additional factors influence banking firm values including macroeconomic conditions, regulatory changes, technological capabilities, management quality, and competitive positioning (Martinez & Chen, 2021). Future research should incorporate these dimensions for comprehensive valuation models (Kumar & Singh, 2020).

Conclusion

Based on empirical findings and statistical analyses, this research draws following conclusions:

1. **Investment Decision (PER)** exerts significant positive effect on firm value (t-calculated = 2.630, p = 0.012). Higher Price to Earnings Ratios enhance banking firm valuations by signaling superior growth prospects and profitability expectations to market participants (Hassan & Ahmed, 2022).
2. **Debt Policy (DER)** demonstrates no significant effect on firm value (t-calculated = -0.833, p = 0.409). Leverage variations among Indonesian banking companies do not substantially influence market valuations, potentially reflecting regulatory constraints and sector-specific characteristics (Campbell & Ross, 2023).
3. **Dividend Policy (DPR)** exhibits significant negative effect on firm value (t-calculated = -2.465, p = 0.018). Higher dividend payout ratios reduce firm valuations, suggesting markets favor earnings retention for growth investments over immediate shareholder distributions in banking sector contexts (Chen & Lin, 2021).
4. **Investment decision, debt policy, and dividend policy simultaneously** affect firm value significantly (F-calculated = 8.425, $p < 0.001$), explaining 15.8% valuation variations. This confirms firm value represents multidimensional construct influenced by comprehensive financial strategy considerations (Anderson & White, 2023).

These findings validate Signaling Theory and Trade-Off Theory applications in banking sector financial decision-making contexts (Turner & Miller, 2022). Results provide valuable insights for corporate managers optimizing financial strategies and investors evaluating banking firm performance (Wilson & Anderson, 2020).

Recommendations

For Corporate Management:

1. Emphasize profitability enhancement and growth opportunity development to strengthen PER positioning and market valuation
2. Maintain optimal capital structures balancing regulatory compliance with operational efficiency
3. Prioritize strategic reinvestment over excessive dividend distributions during growth phases, aligning distribution policies with long-term value creation objectives
4. Communicate financial strategies transparently to reduce information asymmetry and strengthen investor confidence

For Investors:

1. Incorporate comprehensive financial indicator analyses including investment decisions, debt policies, and dividend policies when evaluating banking firm investments
2. Recognize PER significance as reliable indicator of growth potential and profitability expectations
3. Consider dividend policy implications on reinvestment capabilities and long-term value creation
4. Monitor regulatory developments and macroeconomic conditions affecting banking sector valuations

For Future Research:

1. Expand variable scope incorporating macroeconomic factors, corporate governance quality, technological capabilities, and competitive positioning
2. Examine moderating effects of regulatory changes, economic cycles, and industry characteristics on financial policy-firm value relationships
3. Conduct comparative analyses across different banking segments (commercial, Islamic, regional development banks) identifying sector-specific patterns
4. Employ alternative firm value measurements beyond Tobin's Q for robustness verification
5. Extend observation periods capturing longer-term financial policy implications on firm valuation dynamics

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