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The Role of Dividend Policy in Explaining Corporate Governance and Profitability on Firm Value

Yenny Dwi Handayani [a,1,*], **Ewing Yuvisa Ibrani** [b,2*]

[a] Mercu Buana University, Meruya Selatan No.1, 11650, Jakarta, Indonesia
[b] Sultan Ageng Tirtayasa University, Raya Palka Street Km 3 Sindangsari, 42163, Banten, Indonesia
[1] yennydwi.handayani@mercubuana.ac.id*; [2] ewing_ibrani@untirta.ac.id*
*corresponding author

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ABSTRACT

This study aims to determine the effect of corporate governance and profitability on dividend policy based on substitution theory and/or outcome theory in the banking sector in Indonesia. Theoretically, this study contributes which theory is more dominant between substitution theory and outcome theory by linking the influence of corporate governance with dividend policy and providing information about the impact of the application of the theory on firm value and build awareness to be careful of investors. Investors in making investment decisions, especially in the banking industry in Indonesia. In addition, this study also examines the role of dividend policy in explaining the relationship between corporate governance and profitability on the value of banking firms. A sample of 135 observational data comes from 27 banking companies during 2016-2020. This research found that corporate governance has a negative and significant influence on dividend policy. In addition, the CG index is one of the factors that can explain the company's market value. Profitability is empirically proven to influence dividend policy. Dividend policy is proven to play a role in mediating the relationship between profitability and firm value. However, it is empirically proven that dividend policy cannot mediate the relationship between corporate governance and firm value.

1. Introduction

This study aims to determine the effect of corporate governance on dividend policy based on substitution theory and/or outcome theory. Substitution theory recognizes that companies with bad corporate governance practices will improve their image by providing high dividends to shareholders and in the end will increase the company's value for investors (Jiraporn & Ning, 2011; Renneboog & Szilagyi, 2020). On the other hand, outcome theory explains that good corporate governance will impact the shareholders' welfare. The better the implementation of corporate governance, the higher the shareholders' welfare (Kowalewski et al., 2007; La Porta et al., 2000; Mitton, 2004; Rizki & Jasmine, 2018). In addition, this study also aims to examine the role of dividend policy in explaining the relationship of corporate governance to the firm value of Indonesian banking. Firm value is an important concept for investors, because firm value is an indicator for the market to assess the company as a whole (Li et al., 2020; Nurlela & Islahuddin, 2008; Rizki & Jasmine, 2018).

Good company performance gives investors an indication of good prospects in the future (Azmy et al., 2019; Kusuma, 2021; Nugroho, 2021). Financial ratios can measure company performance, one of which is profitability. Rizki & Jasmine (2018) argue that the higher the profitability ratio, the better the company can earn profits. Therefore, profitability tends to be of interest to investors to determine their investment decisions. In line with Andawasatya, Indrawati, & Aisjah (2017), Cheryta (2017), Nilasari (2019) found a significant positive effect between profitability and firm value. However, conflicting results were found in studies Hunjra, Ijaz, Chani, Irfan, & Mustafa (2014).

Several factors can influence the creation of corporate value. However, this study focuses on corporate governance and dividend policy. Corporate governance and dividend policy are very important to study in relation to firm value (Malavia Mardani et al., 2018; Setiawan & Phua, 2013). In addition, the implementation of corporate governance in Indonesia is still low, so companies compensate for high dividend policies to cover bad corporate governance (Kartika & Utami, 2019; Sardiyo & Martini, 2021; Sugiyanto & Setiawan, 2019; Wahyuni & Utami, 2018). It can confirm that substitution theory applies in the relationship between corporate governance and dividend policy.

The application of the substitution theory will certainly be very dangerous for investors. Compensation for high dividend policies is used as a mask by companies to increase the profile and value of the company in the eyes of investors and to cover up poor implementation of corporate governance, weak law enforcement, accounting standards, and financial audits that are not yet established, neglect of minority rights and weak supervision of commissioners within the company. If this is allowed, investors will be deceived and may experience losses because the role of corporate governance is the key to the success of a company to grow and be profitable in the long term (Daniri, 2005; Jiraporn & Lee, 2018; Kartika & Utami, 2019). If the outcome theory applies, dividend policy serves as evidence that dividend policy is a factor that needs to be considered in mediating the relationship between corporate governance and firm value. Following study Herawaty (2008); Malavia Mardani et al. (2018); Sofiamira & Asandimitra (2017); Sugiyanto & Setiawan (2019); Yuliyanti (2019), found that corporate governance has a positive effect on firm value.

Therefore, various studies are needed that describe the negative consequences of a weak governance system and try to identify the determinants that can improve the implementation of corporate governance. Measurement with an index is also needed to determine whether the implementation of corporate governance is good or bad. This study uses the Transparency and Disclosure Index (TDI) adopted from the research of Kowalewski et al. (2007). Setiawan & Phua (2013) used TDI to measure corporate governance.

Dividend policy is another important factor to study because dividends can attract investors to increase company value (Jiraporn & Lee, 2018; Jiraporn & Ning, 2011; Malavia Mardani et al., 2018; Renneboog & Szilagyi, 2020). Based on this, this study uses dividend policy as an intervening variable. Because it is expected that dividend policy can mediate the relationship between corporate governance and firm value. When the substitution theory applies, a high dividend policy can increase the firm value even though the company has poor corporate governance implementation. It's because dividends are important for investors, especially in countries with poor corporate governance practices (Jiraporn & Ning, 2011; Mitton, 2004).

There are still inconsistencies in the results of previous studies that make researchers interested in re-examining the effect of corporate governance, profitability, and dividend policy on firm value. Considering corporate governance, profitability is a factor that influences firm value and at the same time affects dividend policy, so in this study dividend policy was chosen as a mediator. This study took samples from the banking industry according to suggestions from previous research (Keumala Sari & Fakhruddin, 2016).

This research contributes theoretically about which theory is more dominant (substitution theory or outcome theory) that applies in Indonesia by linking the influence of corporate governance with dividend policy and provides information about the impact of the application of the theory on firm value and building awareness to be careful. Investors make investment decisions, especially in the banking industry in Indonesia. In addition, this study aims to determine how the role of dividend policy in providing a mediating effect in explaining the relationship between corporate governance and profitability on the value of the banking sector in Indonesia.

2. Literature Review

Substitution Theory and Outcome Theory

La Porta *et al.* (2000) stated that two theories show the relationship between the level of corporate governance implementation and dividend distribution: outcome theory and substitution theory. Substitution theory explains the negative relationship between corporate governance and the dividend policy taken by the company. The substitution theory states that companies with poor corporate governance practices try to improve their image by providing high dividends to shareholders. They hope this action will incentivize investors to continue investing in them. This will also increase the profile and value of their company among investors. This theory is supported by research conducted by Jiraporn & Ning (2011); Renneboog & Szilagyi (2020).

Meanwhile, the opposite of substitution theory is outcome theory. Outcome theory states that there is a positive relationship between corporate governance and dividend policy, where the better the company's corporate governance practices, the greater the number of dividends distributed. According to outcome theory, the implementation of good corporate governance will have an impact on the welfare of shareholders. The better the implementation of corporate governance, the higher the welfare of shareholders (Kowalewski et al., 2007; La Porta et al., 2000; Mitton, 2004; Rizki & Jasmine, 2018).

Firm Value

Several concepts explain firm value, namely market value, book value and intrinsic value (Ohlson, 1995; Wibowo et al., 2019). Wibowo et al. (2019) explain that the relationship between market price and book value per share can also be used as an alternative approach to determining the value of a stock, because theoretically the market value of a stock must reflect its book value. So one of the alternatives used in measuring the firm value is the price to book value (PBV). PBV is a comparison of the market price of a stock with its book value. What is meant by book value is the ratio between capital and the number of shares outstanding.

The increasing prosperity of shareholders also increases investors' perceptions of the company's performance and prospects in the future so that investors' perceptions of the company increase. A high PBV value will make the market believe in the company's prospects. On the other hand, if the PBV value is below one, it reflects the company's inability to create a higher value for the company for the amount of capital invested and a decrease in the welfare of shareholders (Martikarini, 2013; Ohlson, 1995; Wibowo et al., 2019).

PBV is the most appropriate measurement used in measuring company value. This is because PBV is a more accurate measurement of how effectively management can utilize economic resources in its policies to make decisions (Nurlela & Islahuddin, 2008; Sutomo & Budiharjo, 2019; Wibowo et al., 2019).

Research Framework

This study aims to examine the effect of corporate governance on dividend policy by linking the applicability between the two theories, namely the substitution theory and the outcome theory. After knowing the applicability of one of the two theories, examine the mediating effect of dividend policy in explaining the relationship between corporate governance and firm value. Because if the substitution theory applies, giving high dividends can be misused by companies to cover up poor implementation of corporate governance.

The role of corporate governance is the key to a company's success in growing and being profitable in the long term (Daniri, 2005). If the outcome theory applies, dividend policy is one of the factors that can be considered in influencing the relationship between corporate governance and firm value.

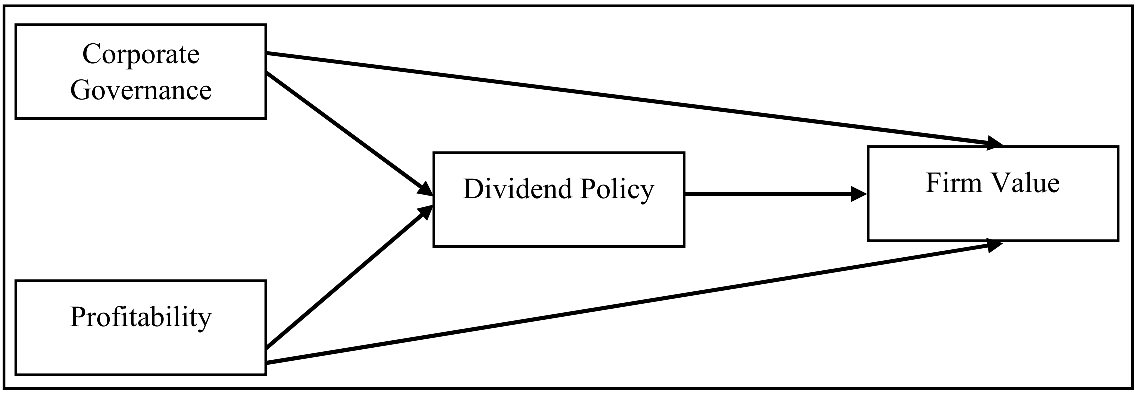

Figure 1. Research Model
Source : developed for this research, 2022

Hypothesis Development

Corporate Governance and Dividend Policy

Good corporate governance is a form of investor protection against the dividend payout ratio (Hidayat et al., 2018; Jiraporn & Ning, 2011; Jusriani & Rahardjo, 2013). Agency theory explains that the existence of corporate governance serves as a tool to provide confidence to investors that shareholders will receive a return on the funds that have been invested. Corporate governance is related to how investors believe that managers will provide profits and will not make unprofitable expropriations of funds that have been invested by investors (La Porta et al., 2000; Shleifer & Vishny, 1989). Companies implementing corporate governance can significantly increase dividend payments (Kowalewski et al., 2007).

However, based on Setiawan & Phua (2013), two theories explain corporate governance's relationship to dividend policy. First, the substitution theory states that the company will compensate for a high dividend policy to cover the poor implementation of corporate governance. Second, outcome theory explains that the company will provide a high dividend policy if the implementation of good corporate governance. Research in line with this theory includes (Kowalewski et al., 2007; La Porta et al., 2000). Both theories can be identified by linking the influence of corporate governance on dividend policy. If corporate governance harms dividend policy, the substitution theory applies. On the other hand, if corporate governance has a positive effect on dividend policy, the outcome theory applies. The null hypothesis is intended to determine which theory applies to Indonesian banking by examining the effect of corporate governance on dividend policy.

H1: Corporate Governance affects Dividend Policy

Corporate Governance and Firm Value

Agency conflicts resulting from management's opportunism will result in low earnings quality. The low quality of earnings will be able to make decision-making errors for its users, such as investors and creditors, so the company's value will decrease (Herawaty, 2008). Agency problems will indicate that the company's value will increase if the company owner can control management behaviour so as not to waste company resources. So, we need a solution to overcome the agency problem. Corporate governance arises because of the limitations of agency theory in overcoming agency problems (Nuswandari, 2009; Renders & Gaeremynck, 2012).

Hidayat et al. (2018) dan Soniami, Gama, & Astiti (2021) empirically prove that the CG index is one of the factors that can explain the company's market value. Darwis (2012) provides evidence that the low quality of CG harms the stock market and the exchange rate of the country's currency. Herawaty (2008 dan Wibowo et al. (2019) also found a significant effect of CG on the company's market value. Thus, the implementation of good corporate governance in the company will increase the value of the company.

H2: Corporate Governance affects Firm Value

Profitability and Dividend Policy

The company will increase the dividend pay-out ratio if profitability increases. Martikarini (2013) Nilasari (2019) Silaban & Purnawati (2016) managed to provide evidence that profitability affects dividend policy. The same results were also shown by Setiawan & Phua (2013), Forti *et al.* (2015). This can be interpreted that profitability is a determining factor for dividend policy, because dividend payments come from net income generated in one operational period. The greater the profitability obtained by the company, the greater the company's capability to distribute dividends. So, the hypothesis in this study are:

H3 : Profitability affects Dividend Policy

Profitability and Firm Value

The ability of a company to generate profits or profits in a period reflects the company's ability to increase the value, which is reflected in the stock price. The level of profitability is a positive signal for investors in predicting the company's value. So, in other words, it can be explained that the company's value can be reflected in its ability to generate profits. The higher the level of profitability, the higher the value of the company, and vice versa.

The higher the profitability ratio, the higher the company pays dividends. The statement regarding the positive effect of profitability on dividend policy is supported by research conducted by Jusriani & Rahardjo (2013) Martikarini (2013), Setiawan & Phua (2013). This study predicts that profitability affects firm value. This prediction refers to the results of previous research that has proven that profitability has a significant positive effect on firm value (Martikarini, 2013; Ohlson, 1995; Wibowo et al., 2019 Hidayat et al. (2018). This study raised the hypothesis:

H4 : Profitability affects firm value

Dividend Policy and Firm Value

The dividend payout ratio will show the percentage of the company's profit distributed to ordinary shareholders in cash dividends (Hidayat et al., 2018). When the company is experiencing growth, the dividend may be small because it focuses more on accumulating funds, but when it is at maturity (the revenue earned is large enough), while the need for cultivating funds is not so large, the dividend paid can be increased. Paying dividends fairly can help companies attract investors to seek dividends, which can help maintain the company's value. The results expected by investors are in the form of dividends and an increase in the value of shares.

Paying dividends to shareholders will increase the company's value (Baker & Powell, 2012; Jusriani & Rahardjo, 2013; Mitton, 2004). Fama & French (1998) found that investment resulting from dividend policy has positive information about the company in the future, which positively impacts firm value. This is in line with the results of research by Jusriani & Rahardjo (2013) and Martikarini (2013), who found that dividend policy positively affects firm value.

H5: Dividend Policy affects Firm Value

Dividend Policy Mediated Corporate Governance and Firm Value

Based on agency theory, risk-averse agents tend to be selfish and allocate resources from investments that do not increase firm value to more profitable investment alternatives (Herawaty, 2008). Agency problems will indicate that the company's value will increase if the company owner can control management behavior so as not to waste company resources, either in the form of inappropriate investments or shirking (Kawatu, 2009; Siallagan & Machfoedz, 2006).

Corporate governance is a system that regulates and controls companies that are expected to provide and increase company value to shareholders (OECD, 2004). Implementing good corporate governance is believed to increase the company's value. Hidayat et al. (2018) and Malavia Mardani et al., (2018) provided empirical evidence that the overall corporate governance index is important and is one of the causative factors that can explain the market value for independent companies in Korea. Darwis (2012) provides evidence that the low quality of corporate governance in a country has a negative impact on the stock market and the exchange rate of the country's currency during the Asian crisis.

Companies with low corporate governance will compensate for a high dividend policy to raise the profile and value of the company in the eyes of investors so that investors are interested in investing. This can happen because dividend policy is important in reflecting a company's prospects in investors' eyes. This statement is supported by Fama & French (1998) in finding that investment resulting from dividend policy has positive information about the company in the future, which in turn has a positive impact on firm value. This is in line with the results of research by Jusriani & Rahardjo (2013) and Martikarini (2013) founded that dividend policy positively affects firm value.

H6: Dividend Policy Mediated the Relationship between Corporate Governance and firm Value

Dividend Policy Mediated the Profitability and Firm Value

The differences found in previous studies regarding profitability to firm value are a gap for researchers to investigate further. This difference indicates that other factors influence the company's value. Dividend policy is expected to mediate the relationship between profitability and firm value.

Hidayat et al. (2018), Nilasari (2019), Wibowo et al. (2019), in their research provide empirical evidence that profitability has a positive and significant effect on firm value. If the company obtains high profitability, the distribution of dividends will likely be high as well. The large number of dividends distributed will give a signal to investors that the company's capability to generate profits is quite good, this can cause the value of the company to increase. So that the hypothesis built in this study is:

H7 : Dividend Policy Mediated the Relationship between Profitability and firm Value

3. Research Method

This research is quantitative research with a conclusive approach. Conclusive research aims to test and prove something using clear data and specific goals (Yusuf, 2016). This study uses time-series data, namely data collected at a certain point which is used to observe responses in the same period (Supomo & Indriantoro, 2002)

The population in this study was 36 banking companies listed on the Indonesia Stock Exchange for the period 2016-2020. Meanwhile, the sample of companies that would be the object of the study was determined based on the purposive sampling method. Sampling in banking is based on the research advice of Keumala Sari & Fakhruddin (2016), which states that this issue has never been studied. In addition, the phenomenon of many cases regarding the poor implementation of corporate governance in the banking sector in Indonesia.

Operationalization Variables

Firm value, the dependent variable in this study, is proxied by Price to Book Value (PBV). In contrast to Tobin's Q, which has many weaknesses. Agrawal, Monem, & Ariff (1996) stated that PBV is a more valid valuation model for assessing firm value, because PBV has information as the basis for making investment strategies. PBV compares the closing market price of the company's shares at the end of the year with the book value of the shares (Hardiningsih, 2010).

The independent variable used in this study is Corporate Governance which is measured using 32 items of the Transparency and Disclosure Index (Kowalewski *et al*, 2007) which consists of: a). the structure and procedures of the board of commissioners (13 items TDI-Board); b). disclosure of important matters of a company (13 items TDI-Disclosure); c). condition of shareholders in the company (6 items TDI-Shareholders).

This study uses a disclosure scoring approach or dichotomous, i.e., if a company discloses an item on the list, it is given a value of 1 and 0 if it does not disclose (Cooke, 1989). Suppose the value of the Transparency and Disclosure Index is included in the very trusted and trusted category. In that case, implementing Corporate Governance in banking in Indonesia is good. Meanwhile, if it is included in the reliable category, implementing Corporate Governance in banking in Indonesia is bad.

Intervening Variables

This study uses dividend policy as an intervening variable. The dividend policy is proxied by the dividend payout ratio (DPR). DPR is calculated by comparing dividends per share to earnings per share (Amidu & Abor, 2006).

Data analysis

The data analysis used in this research is multiple regression analysis and path analysis. The purpose of using simple and multiple regression analysis is to measure the strength of the direction of the relationship between the dependent and independent variables (Ghozali, 2021). Path analysis uses regression analysis to estimate causality relationships between variables (casual models) that have been previously determined based on theory (Ghozali, 2021).

Hypothesis Test

Regression analysis studies the dependent variable's dependence on the independent variable to estimate and predict the population average or the dependent variable's average value based on the independent variable's known value (Ghozali, 2021). The regression model in this research is:

$$DPR = \beta_0 + \beta_1 TDI + \beta_2 ROA + e \quad (3.1)$$
$$PBV = \beta_0 + \beta_1 TDI + \beta_2 ROA + \beta_3 DPR + e \quad (3.2)$$

where:

PBV = Price to Book Value proxy of firm value
DPR = Dividend Payout Ratio proxy of dividend policy
TDI = Transparency and Disclosure Index proxy of corporate governance
ROA = Return on Assets proxy of profitability

Path Analysis

Path analysis is an extension of multiple linear regression analysis, or path analysis is the use of regression analysis to estimate causality between variables (causal models) that have been determined based on theory. Path analysis alone cannot determine cause-and-effect relationships and cannot be used as a substitute for researchers to see causality relationships between variables. Causality relationships between variables have been formed by models based on theoretical foundations (Ghozali, 2021).

Path analysis by determining the pattern of relationships between three or more variables and is not used to confirm or reject the imaginary causality hypothesis (Ghozali, 2021). According Baron & Kenny (1986) and Ghozali (2021), a variable is called a mediator if the variable influences the relationship between the independent and dependent variables.

4. Results and Discussion

Based on the sampling method and the sampling criteria that have been determined for banking companies listed on the IDX. A total of 27 sample companies was selected for the 2016-2020 period. So that the total number of observations for the sample companies is 27 x 5 observation periods, then 135 observation data are obtained.

Table 4.1. Criteria sample selection

Criteria	Number
Banking companies listed on IDX	36
Companies that do not present consecutive, routine and consistent annual reports during 2016-2020	(9)
Number of companies sampled	27
Observation year	5
Final Sample	135

Source : Secondary data processed, 2022

Table 4.2. Descriptive statistics

Variable	Min	Max	Mean	SD
Corporate Governance (TDI)	0.53	0.69	0.6179	0.03427
Profitability (ROA)	-7.79	27.67	1.5875	2.67584
Dividend Policy (DPR)	0.00	0.75	0.1575	0.16634
Firm Value (PBV)	-1.74	14.72	1.8715	1.62197

Source : Secondary data processed, 2022

Based on table 4.2, the corporate governance (TDI) variable has a mean value of 0.617, meaning that 19 to 20 items in the annual financial statements fall into the TDI index category. This shows that the average banking company in Indonesia is included in the trusted category. The results that are quite reliable are not the expected results for the assessment of corporate banking governance.

Profitability (ROA) has an average value of 1,587. These results indicate that the average banking company in Indonesia has a net profit greater than the company's total assets. The dividend policy (DPR) has an average value of 0.157, meaning that the average banking company in Indonesia pays dividends to shareholders of 15.75%.

Firm value (PBV) has an average of 1.8175. This means that the company's value in the banking sector in Indonesia, which is the study's sample, has an average value of above one. If the PBV value is more than one, it indicates that the company is in an overvalued condition, which means that its shares are valued higher than their book value (Gujarati, 2021). This shows that the banking sector in Indonesia is in a condition that is quite favorable to its shareholders.

Table 4.3. Goodness of Fit result

Model	R Square	Adjusted R Square	F	Sig
1	0.239	0.193	5.829	0.001
2	0.117	0.093	4.963	0.009

Source : Secondary data processed, 2022

The coefficient of determination test (R^2) essentially measures how well the model's ability to explain the variation of the dependent variable is. The value of the coefficient of determination is between zero and one. A small value of R^2 means that the ability of the independent variables to explain the dependent variable is very limited. A value close to one means that the independent variables provide almost all the information needed to predict the variation of the dependent variable (Ghozali, 2021).

Based on the test results shown in table 3, model one shows the value of R-square (R^2) of 0.239, this means that 23.9% of the variation in dividend policy (DPR) can be explained by variations of the three independent variables Corporate Governance (TDI), and profitability (ROA). While the rest (100% - 23.9% = 76.1%) is explained by other reasons outside the model. The calculated F value of this study is 5.829, and the significance is 0.001. Thus, it means that the representation of Corporate Governance (TDI) and profitability (ROA) is empirically proven to have a significant effect on the dependent variable, namely dividend policy (DPR). Likewise, equation two shows the value of R^2 of 0.117, indicating that the variation in firm value (PBV) can be explained by variations in the independent variables of Corporate Governance (TDI), Profitability (ROA), and dividend policy (DPR) of 11.7%. At the same time, other factors outside the model explain the remaining 88.3%. The calculated F value of this study was 4.963 with -value < 0.05. It means that the representation of Corporate Governance (TDI), Profitability (ROA), and dividend policy (DPR) is empirically proven to have a significant effect on firm value (PBV).

Regression Analysis

The regression model used in testing the hypothesis is a multiple regression model to analyze the relationship between two or more independent variables. The results of the research regression analysis are as follows:

$$LnDPR = 1.619 - 5{,}059\ TDI + 0{,}183\ ROA + \varepsilon \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots (4.1)$$

$$LnPBV = 2{,}361 + 2{,}686\ LnTDI + 0{,}010\ ROA + 0{,}365\ LnDPR + \varepsilon \ \ldots.. (4.2)$$

Table 4.4. Regression analysis results

Model	Variable	B	SD	t	Sig.
1	(Constant)	1.619	0.977	1.658	0.102
	CG (TDI)	-5.059	1.595	-3.173	0.002
	ROA	0.183	0.061	3.003	0.004
2	(Constant)	2.361	0.647	3.648	0.000
	LNTDI	2.686	1.198	2.243	0.028
	ROA	0.010	0.004	2.398	0.019
	LNDPR	0.365	0.137	2.666	0.009

Source : Secondary data processed, 2022

Based on the test results of equation 1 (in table 4.4), the constant value (DPR = 1.619) means that if the independent variable consisting of Corporate Governance (TDI) and profitability (ROA) is considered constant or does not change, the amount of dividend policy is 1.619. Thus, Corporate Governance (TDI) has a coefficient with a negative direction while the profitability variable (ROA) has a regression coefficient with a positive direction. Companies with low Corporate Governance (TDI) will increase their dividend policy. Meanwhile, companies with high profitability (ROA) will increase their dividend policy.

Based on the test results of the 2 regression model equations in table 4.4, the constant value (PBV = 2.361) means that if the independent variables consisting of Corporate Governance (TDI), profitability (ROA) and dividend policy (DPR) are considered constant or have not changed, the firm value (PBV) of 2,361. Thus, from these results indicate that the variables Corporate Governance (TDI), Profitability (ROA) and dividend policy (DPR) have a regression coefficient in a positive direction. This means that companies with high Corporate Governance (TDI) and dividend policies (DPR) will increase the firm value.

Corporate Governance on dividend policy

To determine whether the hypothesis is accepted or rejected is to compare t-value with t table and its significance value. Based on the regression test results in table 4.4, the effect of Corporate Governance (CG) on dividend policy shows a t-value -3.173 with a significance of 0.05. This means that Corporate Governance has a negative and significant influence on dividend policy. Thus, hypothesis 1 which states that Corporate Governance has an effect on dividend policy can be accepted. This also confirms that the substitution theory applies in Indonesian banking. This result confirms the application of the substitution theory, which states that companies with poor corporate governance practices will try to improve their image by paying high dividends to shareholders.

The application of the substitution theory in the influence of corporate governance on dividend policy which states that companies that have poor corporate governance practices will try to improve their image by giving high dividends to shareholders to increase their profile and company value among investors as a warning to investors, especially for investors. Investors who want to invest in the long term should be careful because a high dividend policy compensation does not guarantee that the company's performance runs effectively and efficiently and has good corporate governance implementation.

The high dividend policy is used as compensation by companies to increase the profile and value of the company in the eyes of investors and to cover up poor implementation of corporate governance, weak law enforcement, accounting standards and financial audits that are not yet established, capital markets that are still under-regulated, neglect of minority rights. and the weak supervision of the commissioners within the company. If this is allowed in the long term, investors' hopes of getting a return on the funds they have invested will not be achieved and investors will experience losses. The results of this study are consistent with the results of research conducted by Jiraporn & Lee (2018) and Renneboog & Szilagyi (2020).

Profitability on dividend policy

While profitability (ROA) has a coefficient value of 0.183 and a t-value of 3.003 with a p-value of 0.05. Thus hypothesis 2 can also be accepted. This means that profitability is empirically proven to influence dividend policy in banking companies in Indonesia. The results of this study also show that profitability as proxied by (ROA) has a significant effect on dividend policy. Profitability shows the capital invested in total assets to generate company profits. That is, the higher the level of profitability, the greater the possibility of dividend distribution (Sugiyanto & Setiawan, 2019). Profitability, which is the company's ability to earn a profit, has an effect on dividend policy. Suppose the company has a high level of profitability. In that case, the company will get high profits and in the end the profit available to be distributed as dividends to shareholders will be even greater.

Corporate Governance on Firm Value

Based on the test results of equation 2 in table 4.4 the influence of corporate governance on firm value shows the t-value of 3.884 and p-value 0.05. This means that Corporate Governance positively and significantly affects firm value. Thus, hypothesis 3 which states that Corporate Governance has an effect on firm value can be accepted. This also confirms that Corporate Governance has a direct effect on firm value. A high company value (PBV) will make the market believe in the company's future prospects. This is also the desire of the company's owner, because a high company value indicates the prosperity of shareholders is also high (Jiraporn & Lee, 2018). So that the larger the size of the company, the easier it will be to obtain external funding sources which will ultimately increase the company's value (Hardiningsih, 2010).

Solikatun & Dewayanto (2020) proved that the CG index is one of the factors that can explain the company's market value. Study Reilly et al. (2007) provide evidence that the low quality of corporate governance has a negative impact on the stock market and the exchange rate of the country's currency. Silveira dan Barros (2016) also found a significant influence of corporate governance on the company's market value. Hastuti (2005) states that corporate governance refers to a framework of rules and regulations that allow stakeholders to make maximize firm value and returns.

Profitability and Firm Value

Profitability as proxied by ROA on firm value (PBV) shows a t-value 2.398 and p-value 0.05 (in table 4.4). This means that profitability has a positive and significant effect on firm value. Thus, hypothesis 4 which states that profitability is empirically can affect on firm value is acceptable. Profitability is still investors' main information and consideration in predicting firm value. The firm value can be reflected in the company's ability to generate profits. The higher the level of profitability, the higher the value of the company, and vice versa.

Profitability is a measure of the effectiveness of the company's management by management. Effective management of the company by management will produce optimal profits for the company and indirectly increase shareholders' profits. The statement regarding the positive effect of profitability on dividend policy is supported by research conducted by Jusriani & Rahardjo (2013) Martikarini (2013), Setiawan & Phua (2013). This study predicts that profitability has an effect on firm value. This prediction refers to the results of previous research that has proven that profitability has a significant positive effect on firm value (Martikarini, 2013; Ohlson, 1995; Wibowo et al., 2019 Hidayat et al. (2018).

Dividend Policy on Firm Value

Table 4.4 shows the hypothesis testing regarding the effect of dividend policy on firm value significant at alpha 0.05. This means that dividend policy has a positive and significant effect on firm value. Thus, hypothesis 5 which states that dividend policy has an effect on firm value can be accepted. The company's management decision to distribute dividends is related to how strong the company is in generating profits. If a company can generate large amounts of profit, theoretically the company's ability to distribute dividends is also getting bigger. This illustrates that the future of banking will be quite promising along with the level of banking profitability that is getting better. Therefore, dividends will attract investors to invest in a bank which will directly add to the company's value. The results of this study in line with Jusriani & Rahardjo (2013), Martikarini (2013) which state that dividend policy has a positive and significant effect on firm value.

Path Analysis

$$LnDPR = 1.619 - 5{,}059\ TDI + 0{,}183\ ROA + \varepsilon \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(4.3)$$

$$LnPBV = 2{,}361 + 2{,}686\ LnTDI + 0{,}010\ ROA + 0{,}365\ LnDPR + \varepsilon \ldots\ldots(4.4)$$

According Baron & Kenny (1986), a variable is called a mediator if the variable succeeds in influencing the relationship between the predictor (independent) and criterion (dependent) variables. Based on these results, the sixth hypothesis which states that dividend policy can mediate the relationship of corporate governance to firm value has not been successfully accepted by empirical evidence in this study. The results of this study prove that dividend policy cannot mediate the relationship between corporate governance and firm value. However, corporate governance has a significant indirect effect on firm value through dividend policy (as an intervening). So it can be concluded that there is a partial mediation between the relationship of Corporate Governance to firm value and dividend policy.

Dividend Policy mediated Relationship of Corporate Governance and Company Value

Dividend policy in mediating the relationship between corporate governance and firm value has coefficients of 0.948 with p-value 0,171 > 0.05 (in table 4.5). It is empirically proven that dividend policy can mediate the relationship between corporate governance and firm value. Based on the results of the unstandardized coefficients, a model of the path analysis results can be made as follows:

Table 4.5. Path Coefficients

Path	Coefficient	St. Dev	T Statistics	p-value
CG -> DPR	1.595	0.148	2.810	0.002
CG -> PBV	3.884	0.062	0.312	0.031
CG -> DPR -> PBV	0.948	0.074	1.641	0.171
ROA -> DPR	0.183	0.061	3.003	0.004
ROA -> PBV	0.010	0.255	2.398	0.019
ROA -> DPR -> PBV	1.990	0.219	2.345	0.046

Source : Secondary data processed, 2021

The results of this study prove that dividend policy cannot mediate the relationship between corporate governance and firm value. However, corporate governance has a significant indirect effect on firm value through dividend policy (as an intervening). So, it can be concluded that there is a partial mediation between the relationship of Corporate Governance to firm value and dividend policy.

Dividend Policy mediated Relationship of Profitability and Firm Value

The results of path analysis using the Sobel test show that profitability, as proxied by ROA, has a direct effect on firm value with coefficient 0,183 and significant at alpha 5%. While the indirect effect on firm value is 0.199 with a p-value of 0.046 <0.05 (in table 4.5). Based on these results, the seventh hypothesis that dividend policy can mediate the relationship between profitability and firm value has been successfully accepted by empirical evidence in this study.

Dividend policy is proven to be able to mediate the relationship between profitability and firm value. This indicates that investors prefer dividends, cash on hand, over other forms of wealth. Consequently, the company's stock price will be largely determined by the number of dividends distributed. An increase in dividends will increase the stock price, which will also impact the company's value. The greater the profit allows the company to increase its dividend payout ratio. In line with the test results, the distribution of dividends shows how strong the company is in the welfare of its investors. The results of this study follow research conducted by Sriwahyuni and Wihandaru (2015) which found dividend policy could mediate the effect of profitability on firm value.

5. Conclusion

Based on the results of data analysis and discussion described in the previous chapter, it can be concluded that corporate governance as proxied by the Transparency and Disclosure Index (TDI) has a negative and significant influence on dividend policy. This confirms the application of the substitution theory to banking companies in Indonesia. This means that companies that have poor corporate governance are empirically proven to compensate for high dividend policies. In addition, this study provided empirical evidence that the CG index is one of the factors that can explain the company's market value.

Profitability is empirically proven to influence dividend policy in banking companies in Indonesia. In addition, profitability is still investors' main information and consideration in predicting the firm value.

Dividend policy has a significant effect on firm value. The company's management decision to distribute dividends is related to how strong the company is in generating profits. Therefore, dividends will attract investors to invest in a bank which will directly add to the firm value.

Dividend policy is proven to play a role in mediating the relationship between profitability and firm value. This indicates that investors prefer dividends, cash on hand, over other forms of wealth. Consequently, the company's stock price will be largely determined by the number of dividends distributed. An increase in dividends will increase the stock price, which will also impact the firm value. However, the surprising result is that dividend policy cannot mediate the relationship between corporate governance and firm value. However, corporate governance has a significant indirect effect on firm value through dividend policy (as an intervening).

This study has several research limitations that may weaken the results, namely: The Transparency and Disclosure Index (TDI) indicator from the research of Kowalewski *et al.* (2007) is still unable to contribute items in the Transparency and Disclosure Index (TDI) framework, especially in the context of Indonesia. In addition, this study only uses banking companies as research samples without considering long-term or short-term investment aspects.

So further research is very relevant to add years of observation so that the results are more comprehensive and reflect the actual situation. Future research can also expand the research area by considering long-term investments. Because a high dividend policy can be used to cover bad corporate governance and of course it will have a detrimental impact on investors. It is different for investors who only want to invest for the short term. A high dividend policy is an advantage for investors.

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