

FACTORS AFFECTING FIRM VALUE OF A PROPERTY AND REAL ESTATE LISTED ON THE INDONESIA CAPITAL MARKET

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ABSTRACT

Creating firm value is important for all levels of the company to face the increasing business challenges. This paper is to examine factors affecting the firm value of the property and real estate listed companies on the Indonesia Stock Exchange for the period of 2013-2019. The variables used in this study are agency cost, CEO tenure, and profitability. In the way to determine the variables that have a strong influence on the firm value, 38 companies are used as samples, which are selected by using a purposive sampling technique. This study data were processed by using a panel data regression model. The result denotes that agency cost and profitability have a strong influence on the property and real estate listed companies. CEO tenure does not affect the firm value. These findings point that enhancement in the agency costs and profitability leads to raising market trust in the company which can encourage an increase in company value.

Keywords: agency cost, CEO tenure, profitability, firm value, property and real estate

I. INTRODUCTION

Optimizing company value is the main goal of every firm. The firm value will increase in line with the company's growth because it is managed well by the company's management. Company value not only reflects the performance of a company but also describes the company's prospects in the future. Firm value is also associated with the market value of the company's debt and outstanding shares (Camfield & Franco, 2019). Firm value is can relate to the firm stock prices because it describes investor trust in company success. A step-up in company value is influenced by the company's stock value enhancement at the market that will drive shareholder wealth (Rappaport, 1998; Black & Wright, 2001; Handriani & Robiyanto, 2018; Bala et al., 2020). There is a lot of literature that describes the change in firm value as a result of various internal company factors such as agency cost, CEO tenure, and profitability, but the study finding is still mixed (Xiao & Zhao, 2012; Wardani & Susilowati, 2017; Sheikh, 2018; Osasere & Ayo, 2020; Riahi-Belkaoui, 1999; Sucuahi & Cambarihan, 2016; Mubyarto, 2020).

Some financial works of literature explicate that one of internal company variable can effect firm value is agency cost. Discussions about agency costs arise when there is a separation of responsibilities between the agent as the manager of the company and the principal as the owner of the company. Agency costs are present as costs that must be incurred by the principal in order to monitor the agent's work so that it is in accordance with the agreed contract due to the separation of responsibilities that creates a conflict of interest (Jensen & Meckling, 1776). They further mention that this costs are inevitable when there is a separation between ownership and control, and refer to these costs as "inefficiency". In the company's business operations, it is often found that agents act for their interests which are not profitable for shareholders, that encouraging higher conflicts of interest which can lead to high agency costs and will affect the value of the company (Zakaria, et. al., 2016). The relationship between agency cost and firm value can be positive as found by Osasere & Ayo (2020) by using asset utilization ratio as a measurement of agency cost. Meanwhile, other researchers were found that agency costs have a negative effect on the firm value (Lemmon & Lins, 2003; Bennedsen & Nielsen, 2010).

CEO has an important role in influencing the company's business operations. The relationship amongst CEO tenure and company value is still a debate in the financial literature. Several academics express ambiguous opinions and argue that there is no connection between CEO tenure and firm value (Hermalin & Weisbach, 1998; Garrett & Pavan, 2012). Some empirical evidence shows that the results obtained by companies vary concerning the CEO's time in office (Ali and Zhang, 2015; Pan et al., 2016). This evidence shows that the link between CEO tenure and firm value is still unclear. At the beginning of his tenure in the company, the market will observe the CEO's

competence and will react to the CEO's potential to manage the company which is reflected in the company's earnings report (Ali, & Zhang, 2015). Brochet et. al. (2019; Mosala & Chinomona, 2020; Bello & John, 2020; Kayaalp et al., 2020) found that CEO tenure is closely connected to the suitability of the CEO's in the company which can cause an increase or decrease in the value of the company. Another variable is profitability there has been a lot of research on its relationship with firm value. Profitability shows the company's power to generate profits by employing all company assets (Shapiro, 1991; Husnan, 2001). Profitability is often used as a reference by several investors to estimate the company's potential in the future. Some of the researchers found that profitability has positive correlation toward the firm value (Hermuningsih, 2013; Naceur & Goaid, 2002).

Refer to the above explanation, this paper aim is to examine factors affecting the firm value (agency cost, CEO tenure, and profitability) of the property and real estate listed companies for the period of 2013-2019 and found the powerful factors that influence value of company. This study is different from previous studies, since the use of agency cost and CEO tenure variables that both of the finding results are still being debated and unclear.

II. LITERATURE REVIEW AND HYPOTHESES DEVELOPMENT

Agency Cost and Firm Value

Agency theory continues to progress from time to time. The modern agency theory is growing, majority adopted from the work of Mitnick, 1973 and Ross, 1973, covering the fields of political science and economics. However, despite this, much previous work on the analysis of economic risk and the mismatch of individual and group goals has redounded to its evolution (eg Arrow 1985; Wilson 2006). The management literature portray that the principles of agency theory have been adopted and developed by Eisenhardt (1989); Jensen and Meckling (1976). The relationship between agents and principals within the firm and the costs associated with contracting these relationships have been widely discussed in the corporate finance literature following Jensen and Meckling (1976). Agency cost arising from conflict of interest among management and owner and will affect firm value (Florackis, 2008). In an agency relationship, the principal will attempt to minimize agency costs, such as deciding, rewarding, and monitoring the behavior of the agents, whilst the agent is on duty to maximize appreciation and reduce the principal's control (Fayezi et al., 2012). Agency costs are grouped into three main costs, namely monitoring costs, bonding costs, and residual loss (Jensen & Meckling, 1976). Monitoring costs include audit fees, writing executive compensation agreement, and the cost of dismissal managers will be fully paid by the principals. Bonding fees are incurred to ensure that the manager's actions will not harm the shareholders' wealth and to insure that the shareholder will be indemnity if he or she is harmed by the agent's actions, however, nevertheless, it cannot be zero cost for the principal or the agent (Jensen & Meckling, 1976). Residual loss is a cost that arises because the cost to fully enforce the contract between the principal and agent will be more profitable. They further mention that this cost is inefficiencies, although it cannot be avoided due to the segregation of principal and management.

Several studies attempt to extend the agency theory model and found that when there is a separation between ownership and management, it has the potential to reduce the value of the company (Grossman & Hart, 1988; Harris & Raviv, 1988; Bennedsen & Nielsen, 2010). Agency cost has a positive effect on firm value, imply that the higher the agency cost, then the manager's activities more controllable that can improve the company's reputation and value (Adityamurti and Ghazali, 2017; Wardani and Susilowati, 2017), while another study finding mention that firm value affected negatively by an agency cost (Lemmon & Lins (2003); Bennedsen & Nielsen (2010); Mustapha & Che, 2011).

H₁: Agency cost effect positively on firm value of property and real estate listed companies

CEO Tenure and Firm Value

The CEO has an important role and influences firm decision, earning, and performance with their better experience and education background (Serfling, 2014; Malekzadeh, et. al., 1998; Pathan, 2009). CEOs with long tenures have an information advantage and participate in decision-making. (Cronqvist & Fahlenbrach, 2009) found that experienced CEOs can improve organizational efficiency and resource allocation in the company. Suitable resource allocation can help companies face competition in the industry with innovative products and different business models to develop a better competitive advantage. The existence of a CEO who has expertise is expected to adequate to maximize the company value taking into account its ability to match the needs of the company that depends on the company's economic environment, especially industrial and technological conditions (Eisfeldt and Kuhnen, 2013).

During the CEO tenure, the company can overcome uncertainty about the quality of the CEO (Pan et al., 2015, Carter et al., 2019), along with the changing environment and increasing competition, the company's capabilities need to change which causes the CEO's expertise to be no longer optimal (Miller, 1991, Garrett and Pavan, 2012, Eisfeldt and Kuhnen, 2013). The new CEO is believed to be able to face challenging conditions, so that it can intensify market reliance which can increase the firm's value if compared to CEOs with long tenure because of his ability and courage to solve problems in uncertain conditions by providing good information about the company's earnings (Geertsema, Lont, & Lu, 2015). CEOs with longer tenures and older ages are believed to be able to draw more consistent conclusions than younger individuals cognitively (Hess, 2006). Short CEO tenure at a young age will be more aggressive in improving their performance because it is closely related to their selling value in the manager's market, therefore high performance has a positive relationship with CEO financial benefits (Boschen et. al. (2003). CEO tenure can have a negative relation with firm value when a long tenure causes the CEO to lose the qualities needed by the company (Bertrand and Mullainathan, 2003; Coles et al., 2014). Laux (2008), mention that CEO tenure and firm value has a positive link on the early year CEO appointment because it is strengthened by CEO knowledge.

H₂: CEO Tenure has a negative relation with firm value.

Profitability and Firm Value

Profitability describes the achievement of company profits by using all company assets during a certain period (Husnan, 2001). Profitability has a prominent part in the firm because it is one indicator that points to the company's achievements as well as reflects the company's prospects in the future (Hermuningsih, 2013). The company's business sustainability is also determined by the increase in the company's profitability. Profitability also provides an indication of management performance in managing the company (Petronila and Mukhlisin, 2003). (Naceur dan Goaid, 2002) mention that profitability can be considered as a very important driving factor for firm value. The increase in company performance will be reflected in the increase in company profitability which can increase market confidence in the company so that it can encourage an upgrade in firm value (Suharli, 2006). Profitability has a function as a value driver and value creation for firm value (Rappaport (1986).

Several studies found that firm value has a positive relationship with profitability (Naceur & Goaid, 2002; Harmuningsih, 2014; Sucuahi & Cambariham, 2016). Another paper indicates that profitability has a negative connection on the firm value of the property and real estate listed firms.

H₃: Firm value is positively affected by profitability

Research Method

This research is applied study that uses a quantitative method and secondary data to determine the factors that affect the firm value. The data uses in this study gathered from the official website of the Indonesia capital market and other relevant sources. The population of this paper is property and real estate companies listed in Indonesia with a total of 45 companies. Thirty-eight companies' uses as samples that were choose with certain criteria techniques from 2013 to 2019. Four variables use to achieve this study aim that consist of firm value (FV) as dependent variable and agency cost (AC), CEO tenure (CT), and profitability (PR) as independent variables.

Firm value measure by using Tobin's Q (market capitalization added debt and divided total asset) as used by Wei & Varela, 2003; Osasere & Ayo, 2020. While, agency cost measure by using total sales divided total asset, CEO tenure calculated by using The number of years as CEO in the firm, and the last, profitability be sought by using return on asset (net profit divided total asset).

This study adopted a panel data regression model to test the link among of agency cost, CEO tenure, and profitability with the firm value of the property and real estate listed firm. Regression model of this paper as below equation 1:

$$FV = a + \beta_1 AC + \beta_2 CT + \beta_3 PR + e$$

Where FV is firm value, CT is CEO tenure, and PR is profitability as variables used in this study. Pane data regression test start from classical assumption test consists of multicollinearity test and heterokedasticity test. Before testing the hypothesis, a model test (F test) is conducted to ensure that the regression model formed is

correct. Hypothesis tests were carried out to answer each hypothesis proposed in this study with an error rate of 5%.

III. RESEARCH RESULT AND DISCUSSION

Results

The results of the panel data regression test denote that the regression model formed is free from multicollinearity problems as seen from the VIF value of each variable less than 10 and does not have heteroscedasticity problems as reflected by the P-value obs * R-square > 0.05 using the Breusch-Pagan-Godfrey approach. The panel data regression model used is a random effect because the amount of cross-section data used is more than the time series as mention by (Nachrowi and Usman, 2006). The panel data regression test finding indicated that the regression model that was formed was correct with the prob F-statistic value <0.05. Its means that the independent variables used in the analysis (AC, CT, and PR) have a linear relationship with the dependent variable (FV). Table 1 below presents the results of panel data regression and multicollinearity test.

Table 1, Random Effect and Multicollinearity Output Test

Independen Variables	Value	VIF
AC	1.426507**	1.251080
CT	-0.002643	1.006632
PR	2.567573**	1.252225
Adjusted R ²	0.077864	
F-statistic	8.458732	
F-statistic sig.	0.000022	

** sig. at 5%

Source: financial report , data processed

The statistical tests outcomes as shown in table 1 above points that agency costs and profitability have a positive influence on the company value of the property and real estate listed firm during 2013 – 2019 period. Meanwhile, CEO tenure has no connection with firm value.

Discussion

The separation of responsibilities between the principal and the agent has created a conflict of interest which has led to the emergence of agency costs. A high agency cost is indicating that the costs for monitoring agent actions are under the contract and the principal's interests. Empirical statistics output denote that agency cost has a positive relationship with value of firm. The higher of the agency cost, then more efficient the agent in managing the company, so that it can increase the value of the company and the principal's welfare. Strict control over agents can improve the performance of agents and perform in the interests of the stockholderl as stated in the cooperation agreement among the management and the owner. This study finding is in line with the study outcomes of Adityamurti and Ghozali, 2017; Wardani and Susilowati, 2017. This research finding is not in line with Lemmon and Lins (2003); Bennedsen and Nielsen (2010); Mustapha & Che, 2011 who found that agency costs have a negative relationship with firm value.

CEO tenure is also expected to have a close link with the value of the firm although the relationship is still unclear. A long-term CEO tenure does not guarantee that a CEO can meet the qualifications required by the company. CEOs that are not qualified will be replaced by principals and their selling value in the manager's market will decrease. The new CEO is believed to be able to face challenging conditions, so that it can upgrade market trust which can increase the value of the firm if compared to CEOs with long tenure because of his ability and courage to solve problems in uncertain conditions by providing good information about the company's earnings (Geertsema, Lont, & Lu, 2015). Hypothesis test result point that firm value is not affected by CEO tenure. This finding shows that CEO tenure does not determine the increase or decrease in the value of the company. Investors do not use CEO tenure as a basis for trust in the company's performance but pay more attention to the company's work which is reflected in the company's earnings that continue to increase. The quality of a CEO's work is not seen from CEO tenure but from the skills he has and his speed in learning to face the challenges of an increasingly high industry in

an uncertain environment. This research finding does not support to study result of Bertrand and Mullainathan, 2003; Coles et al., 2014; Laux, 2008.

Profitability has a notable role in the firm business activities because it is one indicator that points to the company's achievements as well as reflects the company's potential in the future. High profitability can assure the firm's business continuity. Empirical findings indicate that profitability has a positive connection with firm value. This result point that the higher level of profitability, then higher value of the company. High profitability reflects the success of management in utilizing the company's assets maximally. This condition encourages higher market confidence in the company, which is reflected in the increase in the company's share price and causes the firm's value to work up. This paper finding is in line with study performed by Naceur & Goaid, 2002; Harmuningsih, 2014; Sucuahi & Cambariham, 2016.

Research Conclusion

This paper was set to analyze factors affecting the firm value of the property and real estate listed companies in the Indonesia during 2013-2019 by using agency cost, CEO tenure, and profitability as independent variables. Research findings receive that firm value affected by agency cost and profitability positively. Research result reveals that CEO tenure affects the firm value. The overall results of this study imply that agency costs and profitability play a role in increasing firm value. Agency cost illustrates that the monitoring carried out on agents is efficient in encouraging the improvement of management's skills to manage the company. Profitability shows that management can manage the company's assets well, thereby providing confidence to investors about the company's sustainability and potentials in the future.

Refer to this overall finding, this study still has some limitations, thus further studies should use another variable that has a strong relationship with firm value based on relevant literature review, with a long period of study and variety industry.

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