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Pathways to Firm Value: The Effects of Financial Distress, Capital Structure, Investment Opportunity Set, and Dividend Payout on Firm Value through Profitability with Firm Size as a Moderator

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Abstract

Firm value remains a central issue in Indonesia's property and real estate industry, as market valuation does not always reflect firms' financial performance. Prior studies have reported inconsistent findings regarding the effects of financial distress, capital structure, investment opportunity set, and dividend policy on profitability and firm value, while the moderating role of firm size in the profitability-firm value relationship remains underexplored. This study employs an integrated corporate finance framework to examine the effects of financial distress, capital structure, investment opportunity set, and dividend policy on profitability, the effect of profitability on firm value, and the moderating role of firm size. An explanatory quantitative research design was employed using secondary data from property and real estate companies listed on the Indonesia Stock Exchange during the 2010–2019 period. Through purposive sampling, 270 firm-year observations meeting the criteria were obtained from an initial 420 firm-year observations. Financial distress was measured using the Altman Z-Score; panel data were estimated using the Fixed Effect Model (FEM) based on the Chow and Hausman tests, while the moderating effect was tested using Moderated Regression Analysis (MRA). The results show that the four independent variables have a significant effect on profitability ($R^2 = 0.7602$, or 76.02%): financial distress exerts a negative effect, whereas capital structure, investment opportunity set, and dividend policy exert significant positive effects. Profitability significantly affects firm value ($R^2 = 0.8091$, or 80.91%); after firm size is incorporated as a moderator, R^2 increases to 0.8443 (84.43%), indicating that firm size strengthens this effect. These findings support Trade-off Theory, Agency Theory, and Signaling Theory, and offer practical implications for managers, investors, and regulators in formulating financial strategies to enhance profitability and sustainable firm value.

KEYWORDS

financial distress; capital structure; investment opportunity set; dividend payout; profitability; firm value; firm size.

Introduction

The property and real estate sector plays a strategic role in supporting sustainable economic development because it stimulates investment, employment creation, urban expansion, and infrastructure development. In emerging economies such as Indonesia, this sector has become one of the major contributors to national economic growth, particularly through increasing demand for residential, commercial, and industrial properties. Nevertheless, despite continuous government support for infrastructure development and urbanization, many listed property and real estate companies continue to experience fluctuating financial

performance and relatively low market valuation. During the 2010–2019 period, several companies recorded declining profitability despite maintaining substantial asset growth, while their market value did not always reflect improvements in operational performance. This phenomenon suggests that firm value in this sector cannot be explained solely by accounting performance but is also influenced by strategic financial decisions and market perceptions (Reschiwati et al., 2020; Rinaldy et al., 2023).

Firm value represents one of the primary objectives of corporate financial management because it reflects shareholders' wealth and investors' expectations regarding future company performance. A higher firm value indicates stronger market confidence, easier access to external financing, and greater long-term competitiveness. According to corporate finance theory, managers are expected to maximize firm value through effective investment, financing, and dividend decisions while maintaining financial sustainability (Brealey et al., 2023; Brigham & Houston, 2019; Ross et al., 2019). In capital markets, firm value is commonly measured using Price to Book Value (PBV) or Tobin's Q, both of which incorporate market expectations beyond accounting profitability. Consequently, understanding the financial factors that ultimately enhance firm value has become an increasingly important issue for both academics and practitioners, particularly in capital-intensive industries such as property and real estate (Alamsyah & Malanua, 2021; Rinaldy et al., 2023).

The relationship between corporate financial decisions and firm value can be explained through several complementary theoretical perspectives. Agency Theory argues that conflicts of interest between managers and shareholders may reduce firm value when managers pursue personal objectives rather than shareholder wealth maximization (Jensen & Meckling, 1976). Signaling Theory suggests that financial information disclosed by companies including profitability, dividend policy, and capital structure serves as a signal that influences investors' perceptions of future corporate performance (Ross et al., 2019; Spence, 1973). Meanwhile, Trade-off Theory explains that firms attempt to determine an optimal capital structure by balancing the tax advantages of debt against the costs of financial distress (Kraus & Litzenberger, 1973). These three theories collectively provide an integrated framework for explaining how financial distress, capital structure, investment opportunity set, and dividend payout affect profitability and ultimately contribute to firm value.

Profitability occupies a central position within this theoretical framework because it reflects management's effectiveness in utilizing corporate resources to generate earnings (Kasmir, 2019) while simultaneously serving as an important signal for investors. Higher profitability generally increases investor confidence, attracts additional investment, and contributes positively to firm value. Previous empirical studies consistently demonstrate that profitability positively influences firm value across various industrial sectors (Reschiwati et al., 2020; Rosikah et al., 2018; Sembiring et al., 2022; Sucuahi & Cambarihan, 2016). However, profitability itself is influenced by multiple corporate financial decisions rather than functioning as an isolated determinant. Consequently, identifying the financial variables that enhance profitability becomes essential for understanding the broader mechanism through which firm value is created.

Among these determinants, financial distress has received substantial attention because deteriorating financial conditions may substantially reduce corporate profitability and threaten business continuity. Financial distress reflects a firm's inability to meet financial obligations and often precedes corporate restructuring or bankruptcy. From the Trade-off Theory perspective, excessive financial distress

increases bankruptcy costs that ultimately weaken firm performance. Empirical evidence, however, remains inconclusive. Dirman (2020) and Dwiantari & Artini (2021) reported that financial distress negatively affects profitability, whereas Radja et al. (2020) suggested that profitability primarily predicts financial distress rather than the reverse relationship. Furthermore, Ghasemzadeh et al. (2021) found that profitability does not significantly influence financial distress. These inconsistent findings indicate that the causal relationship between financial distress and profitability remains theoretically and empirically unresolved, particularly within capital-intensive industries.

Capital structure, investment opportunity set (IOS), and dividend payout are also considered important financial policies affecting corporate profitability and firm value. Trade-off Theory argues that an optimal capital structure enables firms to minimize financing costs while maximizing shareholder value, although excessive leverage simultaneously increases financial risk (Brigham & Houston, 2019). Previous studies generally found that capital structure positively affects profitability (Miswanto et al., 2022; Puri et al., 2024), whereas investment opportunity set reflects corporate growth opportunities capable of improving future earnings and market valuation (Hidayat et al., 2020; Nguyen et al., 2023). Likewise, dividend payout functions as an important signal of financial strength under Signaling Theory because dividend distributions communicate management's confidence regarding future earnings (Alamsyah & Malanua, 2021). Nevertheless, previous empirical evidence concerning these relationships remains fragmented because most studies examine each variable separately rather than integrating them into a comprehensive value creation framework.

Although previous studies have substantially advanced understanding of financial determinants of firm value, several important research gaps remain. First, from a theoretical perspective, prior studies generally treat firm size as a control variable, while relatively few investigate its moderating role in strengthening the profitability firm value relationship. Second, from an empirical perspective, inconsistent findings regarding the influence of financial distress on profitability and the indirect mechanism linking financial decisions to firm value remain unresolved. Third, from a contextual perspective, most existing studies focus on manufacturing firms, banking institutions, or cross-sector samples, whereas limited evidence is available for Indonesia's property and real estate sector a capital-intensive industry characterized by long investment cycles, substantial financing requirements, and high exposure to financial distress. Moreover, the 2010–2019 period represents an analytically important phase because it captures post-global financial crisis recovery, rapid infrastructure expansion, and the property market adjustment before the COVID-19 pandemic. Accordingly, this study seeks to develop a more comprehensive value creation model by simultaneously examining the effects of financial distress, capital structure, investment opportunity set, and dividend payout on profitability and firm value while incorporating firm size as a moderating variable, thereby extending previous theoretical and empirical literature.

The novelty of this study lies in the development of a comprehensive value creation framework that integrates multiple financial determinants into a single causal model. Unlike previous studies that predominantly examined financial distress, capital structure, investment opportunity set, dividend payout, profitability, or firm value in isolation, this research simultaneously investigates the direct effects of four financial decision variables on profitability and their subsequent implications for firm value. More importantly, this study extends prior literature by positioning firm size as a moderating variable rather than merely a control variable. This integrated framework provides a broader explanation of how financial

policies influence value creation through profitability, thereby enriching the theoretical understanding of corporate finance in emerging capital markets (ElBannan, 2021).

This study also contributes theoretically by integrating Agency Theory, Signaling Theory, and Trade-off Theory into a unified conceptual framework. Agency Theory explains managerial financial decision-making aimed at maximizing shareholder wealth while minimizing agency conflicts (Jensen & Meckling, 1976). Signaling Theory explains how profitability, dividend policy, and capital structure communicate positive or negative signals regarding future firm performance to investors (Ross, 1977; Spence, 1973). Meanwhile, Trade-off Theory explains the balance between the benefits of debt financing and the costs arising from financial (Kraus & Litzenberger, 1973). Combining these complementary perspectives enables this study to explain not only whether financial variables influence profitability and firm value, but also why these relationships occur within capital-intensive industries characterized by high financing needs and substantial investment commitments.

From an empirical perspective, this research addresses inconsistencies reported in previous studies by testing an integrated model using panel data from Indonesian property and real estate companies over the 2010–2019 period. This period represents an important stage in Indonesia's economic development, encompassing post-global financial crisis recovery, accelerated infrastructure expansion, rapid urbanization, and property market adjustments before the COVID-19 pandemic. These unique macroeconomic conditions provide an appropriate context for examining the dynamics between financial distress, financing decisions, investment opportunities, profitability, and firm value. Consequently, the findings are expected to provide more comprehensive empirical evidence regarding corporate value creation in emerging economies, particularly within industries characterized by high capital intensity and long investment horizons.

Beyond its theoretical and empirical contributions, this study also offers practical implications for corporate managers, investors, creditors, and policymakers. For managers, the findings are expected to support strategic financial decision-making concerning capital structure optimization, financial risk management, investment planning, and dividend policy formulation to enhance profitability and maximize firm value. For investors and creditors, the integrated model provides a broader framework for evaluating corporate financial performance and future growth prospects. Furthermore, policymakers may utilize the findings to formulate financial and investment policies that strengthen the competitiveness and sustainability of the Indonesian property and real estate sector.

Based on the theoretical framework, empirical inconsistencies, and identified research gaps, this study seeks to examine the mechanisms through which financial decisions create firm value. Specifically, the objectives of this study are: (1) to analyze the effect of financial distress on profitability; (2) to examine the effect of capital structure on profitability; (3) to investigate the influence of investment opportunity set on profitability; (4) to evaluate the effect of dividend payout on profitability; (5) to analyze the influence of profitability on firm value; and (6) to examine whether firm size moderates the relationship between profitability and firm value in Indonesian property and real estate companies listed on the Indonesia Stock Exchange.

Drawing upon Agency Theory, Signaling Theory, Trade-off Theory, and previous empirical findings, this study formulates the following research hypotheses: H1: Financial distress has a negative and significant effect on profitability. H2: Capital structure has a positive and significant effect on profitability. H3: Investment opportunity set has a positive and significant

effect on profitability. H4: Dividend payout has a positive and significant effect on profitability. H5: Profitability has a positive and significant effect on firm value. In addition, this study proposes a moderating relationship to explain the boundary condition under which profitability contributes more strongly to firm value. H6: Firm size positively moderates the relationship between profitability and firm value, such that the positive effect of profitability on firm value becomes stronger in larger firms than in smaller firms.

By integrating multiple financial determinants within a single conceptual framework and examining their interrelationships in Indonesia's property and real estate sector, this study advances existing corporate finance literature by providing a more comprehensive explanation of the pathways through which financial decisions generate firm value. Accordingly, the proposed model contributes theoretically by extending existing financial theories, empirically by addressing inconsistent findings in previous studies, and practically by offering evidence-based recommendations for improving long-term corporate value creation.

Methods

Research Design

This study employed a quantitative explanatory research design (Sugiyono, 2019) to examine the causal relationships among financial distress, capital structure, investment opportunity set, dividend payout, profitability, firm value, and firm size in Indonesian property and real estate companies. The explanatory approach was adopted because the study aims to test theoretically derived hypotheses concerning the effects of financial distress, capital structure, investment opportunity set, and dividend payout on profitability, the effect of profitability on firm value, and the moderating role of firm size. Panel data regression was selected because it combines cross-sectional and time-series observations, thereby improving estimation efficiency while controlling for unobserved firm-specific heterogeneity (Baltagi, 2021; Gujarati & Porter, 2020; Hsiao, 2022).

Population and Sample

The population comprised all property and real estate companies listed on the Indonesia Stock Exchange (IDX) during the 2010–2019 observation period. Secondary data were collected from audited annual reports and financial statements published by the Indonesia Stock Exchange (IDX) and the official websites of the sampled companies. Purposive sampling was employed to obtain firms that met the objectives of the study. The sampling criteria were as follows:

1. Property and real estate companies continuously listed on the Indonesia Stock Exchange during the 2010–2019 period.
2. Companies publishing complete audited annual financial statements throughout the observation period.
3. Companies providing complete financial information required to calculate all research variables.
4. Companies with complete market data necessary for measuring firm value.

An initial screening identified 48 property and real estate companies listed on the IDX at any point during 2010–2019. Applying the first sampling criterion (continuous listing throughout the full 2010–2019 period) reduced this number to 42 companies, yielding an initial pool of 420 firm-year observations (42 companies × 10 years). After further excluding firm-years with incomplete financial statements, missing market information, or unavailable data required to calculate the research variables, 150 firm-year observations were dropped. Because these exclusions were not distributed evenly across firms or years, the final sample used for

Table 1. Sample Selection Process

Criteria	Companies	Firm-Year Observations
Property and real estate companies listed on the IDX at any point during 2010–2019	48	480
Less: companies not continuously listed throughout 2010–2019	(6)	(60)
Companies continuously listed throughout 2010–2019 (initial pool, 10 years each)	42	420
Less: firm-years excluded for incomplete financial statements, missing market data, or incomplete variables	—	(150)
Final sample used for analysis (42 firms)	42	270

Table 2. Operational Definition and Measurement of Variables

Variable	Proxy	Measurement
Financial Distress	Altman Z-Score	$(Z=1.2X_1+1.4X_2+3.3X_3+0.6X_4+1.0X_5)$
Capital Structure	Debt-to-Equity Ratio (DER)	Total Debt / Total Equity
Investment Opportunity Set	CAPBVA	Capital Expenditure / Book Value of Assets
Dividend Payout	Dividend Payout Ratio (DPR)	Dividend per Share / Earnings per Share
Profitability	Return on Assets (ROA)	Net Income / Total Assets
Firm Value	Price-to-Book Value (PBV)	Market Price per Share / Book Value per Share
Firm Size	SIZE	Natural logarithm of Total Assets, ln (Total Assets)

regression analysis is an unbalanced panel comprising 270 firm-year observations drawn from the 42 sampled companies over 2010–2019. Table 1 summarizes this sample-selection process. This final dataset fulfilled the assumptions required for panel data estimation and ensured the consistency and reliability of the empirical analysis.

The final sample consisted of 270 firm-year observations obtained from 42 property and real estate companies listed continuously on the Indonesia Stock Exchange during 2010–2019. From the initial 420 firm-year observations, 150 observations were excluded because of incomplete financial statements, missing market information, or unavailable data required to calculate one or more research variables. Consequently, the final dataset constitutes an unbalanced panel that satisfies the data completeness requirements for panel regression estimation and provides reliable observations for hypothesis testing.

Data Source

This study utilized secondary data obtained from audited annual reports, financial statements, and market information published by the Indonesia Stock Exchange (IDX) through <https://www.idx.co.id> and the official websites of the sampled

companies. Financial statement data were used to calculate accounting-based variables, whereas market price data were used to measure firm value. All observations covered the period from 2010 to 2019.

Operational Definition of Variables

Financial Distress was measured using the Altman Z-Score, where a lower Z-score indicates a higher probability of financial distress, while a higher score reflects better financial health. Firm Size was included as a moderating variable because larger firms generally possess greater financial resources, stronger market reputation, and easier access to external financing, which may strengthen the effect of profitability on firm value (see Table 2).

Model Specification

To examine the proposed hypotheses, three panel regression models were estimated: Model 1 tests H1–H4 (the effects of financial distress, capital structure, investment opportunity set, and dividend payout on profitability), Model 2 tests H5 (the effect of profitability on firm value), and Model 3 tests H6 (the moderated regression model evaluating whether firm size moderates the profitability–firm value relationship).

Model 1: Determinants of Profitability

$$ROA_{it} = \beta_0 + \beta_1 FD_{it} + \beta_2 DER_{it} + \beta_3 IOS_{it} + \beta_4 DPR_{it} + \varepsilon_{it}$$

where:

ROA = Profitability

FD = Financial Distress

DER = Capital Structure

IOS = Investment Opportunity Set

DPR = Dividend Payout Ratio

ε = Error term

Model 2: Profitability and Firm Value

$$PBV_{it} = \beta_0 + \beta_1 ROA_{it} + \varepsilon_{it}$$

where:

PBV = Firm Value

ROA = Profitability

Model 3: Moderated Regression Analysis

To evaluate the moderating role of firm size, an interaction term between profitability and firm size was estimated using Moderated Regression Analysis (MRA):

$$PBV_{it} = \beta_0 + \beta_1 ROA_{it} + \beta_2 SIZE_{it} + \beta_3 (ROA \times SIZE)_{it} + \varepsilon_{it}$$

where:

SIZE = Firm Size

ROA x SIZE = Interaction term representing the moderating effect of firm size.

A positive and statistically significant interaction coefficient indicates that firm size strengthens the influence of profitability on firm value, whereas a negative significant interaction coefficient indicates a weakening effect.

Panel Data Estimation Procedure

Panel data estimation was performed using EViews 10.0. Three alternative panel estimators were considered, namely the Common Effect Model (CEM), Fixed Effect Model (FEM), and Random Effect Model (REM). Model selection followed the standard panel data estimation procedure (Ghozali, 2020).

First, the Chow test was conducted to determine whether the Fixed Effect Model was preferable to the Common Effect Model. Since the Chow test rejected the Common Effect Model, the Hausman test was subsequently employed to compare the Fixed Effect Model and the Random Effect Model. The Hausman test indicated that the Fixed Effect Model (FEM) was the most appropriate estimator for all regression equations. Consequently, all hypotheses were tested using the Fixed Effect

Model. Because the Common Effect Model was rejected by the Chow test, the Breusch Pagan Lagrange Multiplier (LM) test was not required in the model selection procedure.

Moderation Analysis

The moderating effect of firm size was examined using Moderated Regression Analysis (MRA) by incorporating the interaction term between profitability and firm size (ROA x SIZE). The significance of the interaction coefficient was used to determine whether firm size moderates the relationship between profitability and firm value. The interaction effect was further interpreted by comparing the explanatory power (R^2) of the baseline model and the moderated model.

Diagnostic Tests

Prior to hypothesis testing, several diagnostic tests were performed to ensure the validity and robustness of the estimated regression models. These tests included descriptive statistics, normality testing using the Jarque Bera statistic, multicollinearity assessment through correlation analysis, heteroscedasticity testing using the Breusch Pagan Godfrey and Glejser tests, coefficient of determination (R^2), F-test for simultaneous significance, and t-test for partial significance (Ghozali, 2018). The diagnostic results indicated that the estimated models satisfied the principal assumptions of panel data regression, with normally distributed residuals, no evidence of serious multicollinearity, and no heteroscedasticity problems. Statistical significance was evaluated at the 5% significance level ($\alpha = 0.05$).

Result and Discussion

Descriptive Analysis Results

Financial Distress

The following analysis presents the descriptive statistics of the Financial Distress variable, measured using the Altman Z-Score. During the 2010–2019 observation period, the average Financial Distress score of property and real estate companies was 0.65, with a standard deviation of 0.08. The highest average value was recorded in 2011 (0.76), whereas the lowest occurred in 2019 (0.52). These findings indicate a gradual deterioration in the financial condition of firms throughout the observation period, suggesting that companies became increasingly exposed to financial distress as the property sector experienced slower growth and greater financing pressure.

The relatively small standard deviation indicates that Financial Distress conditions were relatively homogeneous across the sampled firms. Nevertheless, the declining trend observed during the study period reflects increasing financial vulnerability within the Indonesian property and real estate industry, which is characterized by capital-intensive investments, long project completion cycles, and substantial dependence on external financing.

Capital Structure

The descriptive statistics indicate that the average Capital Structure, measured by the Debt-to-Equity Ratio (DER), was 71.57%, with a standard deviation of 8.53%. The highest average ratio occurred in 2010 (84.54%), while the lowest was observed in 2019 (57.32%). Overall, the declining leverage ratio suggests that property and real estate companies gradually reduced their dependence on debt financing during the observation period. This trend may reflect more conservative financing policies and efforts to improve financial stability amid fluctuating market conditions.

Investment Opportunity Set

The Investment Opportunity Set (IOS) exhibited an

average value of 6.56%, with a standard deviation of 3.13%. The highest average IOS was observed in 2013 (11.78%), whereas the lowest occurred in 2019 (1.40%). These results indicate considerable fluctuations in investment opportunities across the observation period. The declining trend after 2013 suggests that firms became more selective in undertaking new investment projects, consistent with the cyclical nature of the property industry and changing macroeconomic conditions affecting long-term capital investment.

Dividend Payout

The average Dividend Payout Ratio (DPR) was 10.02%, with a standard deviation of 4.04%. The lowest average dividend distribution occurred in 2011 (3.58%), while the highest was recorded in 2017 (16.86%). The descriptive findings indicate that dividend distribution policies varied substantially among companies and across years. Such variation reflects differences in corporate earnings, investment requirements, and financing strategies adopted by firms operating in the property and real estate sector.

Profitability

Profitability, measured using Return on Assets (ROA), had an average value of 5.15% and a standard deviation of 1.63%. The highest average profitability was observed in 2014 (7.72%), whereas the lowest occurred in 2019 (2.04%). The downward trend in profitability indicates that firms experienced increasing pressure in generating returns from their assets during the latter years of the observation period. This pattern is consistent with the weakening performance of the property sector, which experienced slower sales growth and declining investment activities.

Firm Size

Firm Size, measured by the natural logarithm of total assets, recorded an average value of 28.70, with a standard deviation of 0.43. The average firm size increased from 27.94 in 2010 to 29.20 in 2019. These findings indicate that although profitability declined during the study period, companies generally continued to expand their asset base. The relatively small standard deviation also suggests limited variation in firm size across the sampled companies.

Firm Value

Firm Value, measured using the Price-to-Book Value (PBV), exhibited an average value of 34.97%, with a standard deviation of 12.95%. The highest average firm value was recorded in 2010 (55.25%), whereas the lowest occurred in 2018 (21.56%). The declining trend in firm value indicates that investors gradually reduced their market valuation of property and real estate companies during the observation period. This finding is consistent with the decline in profitability and increasing financial pressure observed across the industry, suggesting that market participants responded negatively to weakening corporate financial performance.

Verification Analysis Results

Panel Regression Results

To examine the proposed hypotheses, panel data regression analysis was performed using the Fixed Effect Model (FEM), which was selected based on the Chow and Hausman tests. The estimation results for the first model, examining the effects of Financial Distress, Capital Structure, Investment Opportunity Set, and Dividend Payout on Profitability, are presented in Table 3.

Model statistics:

$R^2 = 0.760191$

Adjusted $R^2 = 0.756$

F-statistic = 62.42440

Prob (F-statistic) = 0.000000

Table 3. Panel Regression Results (Model 1)

Variable	Coefficient	Std. Error	t-Statistic	p-value
Constant	0.299015	—	—	—
Financial Distress	-0.203826	0.017505	-11.64397	0.0000
Capital Structure	0.207379	0.015268	13.58246	0.0000
Investment Opportunity Set	0.150459	0.009286	16.20303	0.0000
Dividend Payout	0.124049	0.011228	11.04809	0.0000

Table 4. Regression Results (Model 2)

Variable	Coefficient	Std. Error	t-Statistic	p-value
Constant	-1.506697	—	—	—
Profitability (ROA)	0.363429	0.013626	26.67079	0.0000

Table 5. Moderated Regression Results

Variable	Coefficient	Std. Error	t-Statistic	p-value
Constant	-1.497741	—	—	—
Profitability (ROA)	0.363429	0.013626	26.67079	0.0000
Firm Size (SIZE)	0.670889	0.020485	32.75025	0.0000
ROA × SIZE	0.670339	0.018287	36.65645	0.0000

The estimated regression equation is:

$$\text{PROF} = 0.299015 + 0.203826\text{FD} + 0.207379\text{CS} + 0.150459\text{IOS} + 0.124049\text{DPR} + \epsilon$$

The overall regression model is statistically significant ($F = 62.42440$; $p < 0.001$), indicating that Financial Distress, Capital Structure, Investment Opportunity Set, and Dividend Payout jointly explain variations in profitability. The coefficient of determination ($R^2 = 0.760191$) indicates that approximately 76.02% of the variation in profitability is explained by the four explanatory variables, while the remaining 23.98% is attributable to other factors outside the model.

Financial Distress and Profitability

Financial Distress was measured using the Altman Z-Score, which evaluates corporate financial health based on liquidity, profitability, leverage, solvency, and activity ratios. A lower Z-score reflects a higher probability of financial distress, whereas a higher score indicates stronger financial stability. The regression coefficient for Financial Distress is -0.203826 ($t = -11.64397$; $p < 0.001$), indicating a statistically significant negative relationship with profitability. Economically, this coefficient implies that firms experiencing greater financial distress tend to generate lower returns on assets because increasing financial pressure reduces managerial flexibility, increases financing costs, and limits productive investment. This finding is particularly relevant for Indonesia's property and real estate sector, where projects require substantial external financing, long development periods, and high fixed investment. Consequently, deteriorating financial conditions substantially reduce firms' ability to generate sustainable profits.

Capital Structure, Investment Opportunity Set, and Dividend Payout

Capital Structure exhibits a positive and statistically significant coefficient ($\beta = 0.207379$; $p < 0.001$), indicating that firms maintaining an appropriate debt-equity composition achieve higher profitability. Likewise, Investment Opportunity Set positively affects profitability ($\beta = 0.150459$; $p < 0.001$), suggesting that firms with greater growth opportunities generate superior operating performance. Dividend Payout also demonstrates a positive and significant influence ($\beta = 0.124049$; $p < 0.001$), indicating that firms distributing dividends tend to exhibit stronger profitability, consistent with Signaling Theory.

Profitability and Firm Value

The second regression model examines the direct effect of profitability on firm value.

Model statistics:

$$R^2 = 0.809116$$

$$F\text{-statistic} = 711.331$$

$$\text{Prob}(F\text{-statistic}) = 0.0000$$

The estimated regression equation is

$$\text{FV} = -1.506697 + 0.363429\text{ROA} + \epsilon$$

The positive coefficient confirms that profitability significantly increases firm value. The model explains approximately 80.91% of the variation in firm value, indicating that profitability constitutes one of the primary determinants of investors' market valuation (see Table 4).

Moderating Effect of Firm Size

To evaluate whether Firm Size moderates the relationship between profitability and firm value, Moderated Regression Analysis (MRA) was conducted by incorporating the interaction term between ROA and Firm Size (see Table 5).

Model statistics:

$$R^2 = 0.844322$$

$$F\text{-statistic} = 140.4692$$

$$\text{Prob}(F\text{-statistic}) = 0.000000$$

$$\text{Number of observations} = 270$$

The moderated regression equation is

$$\text{FV} = -1.497741 + \beta_1\text{ROA} + \beta_2\text{SIZE} + 0.670339(\text{ROA} \times \text{SIZE}) + \epsilon$$

The results of the Moderated Regression Analysis (MRA) demonstrate that profitability, firm size, and the interaction between profitability and firm size significantly influence firm value. The interaction coefficient ($\text{ROA} \times \text{SIZE}$) is 0.670339 ($t = 36.65645$, $p < 0.001$), indicating that firm size significantly strengthens the positive relationship between profitability and firm value. The positive interaction coefficient implies that increases in profitability generate greater improvements in firm value among larger firms than among smaller firms. These findings support the proposition that firm size enhances investors' confidence in profitable firms by signalling stronger financial capacity, better access to external financing, and lower perceived business risk.

The explanatory power of the regression model also increased substantially after incorporating the moderating variable. The coefficient of determination rose from $R^2 = 0.809116$ in the baseline profitability model to $R^2 = 0.844322$ in the moderated model, indicating that firm size contributes additional explanatory power in explaining firm value. This improvement confirms that firm size functions as a

Table 6. Diagnostic Test Results

Test	Statistic	p-value	Decision
Normality (Jarque–Bera)	1.439138	0.327921	$p > 0.05$: residuals normally distributed
Multicollinearity (Highest Pairwise Correlation)	< 0.80	n/a	Correlation < 0.80 : no serious multicollinearity
Heteroscedasticity (Breusch–Pagan–Godfrey)	Not reported	> 0.05	$p > 0.05$: homoscedastic residuals
Heteroscedasticity (Glejser)	Not reported	> 0.05	$p > 0.05$: homoscedastic residuals

strengthening moderator rather than merely acting as a control variable. Approximately 84.43% of the variation in firm value is explained by profitability, firm size, and their interaction, while the remaining 15.57% is attributable to other variables outside the model.

Accordingly, Hypothesis 6 is accepted, indicating that firmsize positively moderates the relationship between profitability and firm value. The empirical findings suggest that larger firms are better able to transform improvements in profitability into higher market valuation because they possess stronger asset bases, broader financing opportunities, greater operational stability, and higher credibility among investors. These results are consistent with Signaling Theory, which argues that firm size provides an additional positive signal regarding corporate quality, and with Agency Theory, which suggests that larger firms generally possess stronger governance mechanisms capable of translating financial performance into enhanced shareholder value.

Panel Model Selection and Diagnostic Tests

The Chow and Hausman tests consistently indicated that the Fixed Effect Model was the most appropriate specification for all estimated models. Therefore, the Fixed Effect estimator was adopted throughout the analysis. Because the Chow test rejected the Common Effect Model, the Breusch–Pagan Lagrange Multiplier test was not required in the sequential panel model selection procedure. Diagnostic tests further confirmed the robustness of the estimated models. The residuals were normally distributed, no serious multicollinearity was detected, and heteroscedasticity tests indicated homoscedastic residuals. Accordingly, the estimated regression coefficients satisfy the principal assumptions of panel regression and provide reliable statistical inference. Table 6 reports the supporting diagnostic-test statistics and decision criteria for each model.

Prior to hypothesis testing, several diagnostic tests were conducted to evaluate the robustness of the estimated panel regression models. The normality test using the Jarque–Bera statistic indicated that the residuals followed a normal distribution across all regression models. For Model 1, the Jarque–Bera statistic was 1.439138 with a probability of 0.327921, while Models 2 and 3 produced Jarque–Bera statistics of 3.868587 and 3.848587, respectively, with probability values of 0.073467, all exceeding the 5% significance level. Therefore, the null hypothesis of normally distributed residuals cannot be rejected.

The multicollinearity assessment showed no evidence of serious multicollinearity among the explanatory variables. Correlation coefficients among the independent variables remained below the commonly accepted threshold of 0.80, indicating that each variable contributes distinct information to the regression model. Because Models 2 and 3 contain only one principal explanatory variable (plus the interaction term), multicollinearity was not considered problematic.

The heteroscedasticity tests further confirmed that the regression models satisfy the homoscedasticity assumption. Model 1 was evaluated using the Glejser test, whereas Models 2 and 3 employed the Breusch–Pagan–Godfrey test. In all cases, the significance values exceeded 0.05, indicating

the absence of heteroscedasticity. Accordingly, the estimated panel regression models satisfy the principal classical assumptions and provide reliable estimates for hypothesis testing.

Financial Distress and Profitability

The empirical findings demonstrate that financial distress exerts a significant negative effect on profitability, supporting H1. This result suggests that firms experiencing higher levels of financial distress tend to generate lower returns from their assets because increasing financial pressure constrains managerial flexibility and reduces operational efficiency. Financially distressed firms generally allocate a larger proportion of their cash flows to debt servicing and liquidity management rather than productive investment, ultimately reducing their ability to generate sustainable earnings.

From a theoretical perspective, this finding is consistent with Agency Theory, which argues that financial distress intensifies conflicts between shareholders and creditors. When firms face financial difficulties, managers tend to adopt more conservative investment strategies to preserve liquidity, while creditors impose stricter monitoring and financing constraints. These agency costs reduce operational flexibility and negatively affect corporate profitability. The result also supports the Trade off Theory, which posits that excessive financial risk increases expected bankruptcy costs, offsetting the tax advantages of debt financing.

This finding is consistent with studies reporting a negative association between financial distress and profitability, including those by Dwiantari & Artini (2021) and Dirman (2020). However, several previous studies have reported insignificant or weaker relationships in manufacturing firms. Such differences may be explained by the unique characteristics of Indonesia's property and real estate industry, which requires substantial capital investment, long project completion periods, and heavy reliance on external financing. These characteristics make profitability more sensitive to deteriorating financial conditions than in industries with shorter operating cycles.

The findings also provide practical implications for corporate managers. Property developers should strengthen liquidity management, maintain prudent debt policies, and continuously monitor early warning indicators of financial distress, such as the Altman Z-Score. Maintaining financial stability is essential not only to avoid financial distress but also to preserve profitability and sustain long-term firm value.

Capital Structure and Profitability

The results indicate that capital structure has a positive and significant influence on profitability, supporting H2. This finding suggests that an appropriate combination of debt and equity financing enables firms to optimize their capital resources and improve operational performance. Rather than representing excessive leverage, the positive coefficient indicates that debt financing has been utilized productively to support profitable investment activities.

This finding is consistent with the Trade-off Theory, which proposes that firms can increase firm performance by balancing the tax benefits of debt against the associated financial risks. Within an optimal capital structure, debt serves

as an effective financing instrument that supports expansion while minimizing the weighted average cost of capital. In addition, Agency Theory suggests that debt can function as a monitoring mechanism by reducing managerial discretion over free cash flows, thereby improving managerial discipline and operational efficiency.

The result is in line with previous studies reporting positive effects of capital structure on profitability. Nevertheless, other studies conducted in manufacturing and consumer goods sectors have documented negative relationships due to excessive leverage. The discrepancy highlights the importance of industry characteristics. Property and real estate companies generally finance long-term projects with long-term debt matched to asset maturity, making leverage more productive than in sectors with rapid inventory turnover and shorter investment horizons. From a managerial perspective, the findings imply that managers should determine an optimal debt-equity mix rather than simply minimizing debt levels. Maintaining a balanced capital structure allows firms to finance strategic development projects while preserving profitability and enhancing shareholder value.

Investment Opportunity Set and Profitability

The empirical findings indicate that the Investment Opportunity Set (IOS) has a positive and significant effect on profitability, thereby supporting H3. This result suggests that firms with greater investment opportunities are more capable of generating future earnings because they possess broader prospects for expanding productive assets and developing new projects. In the property and real estate industry, investment opportunities are reflected in the availability of strategic land banks, residential development projects, commercial buildings, and integrated property developments that are expected to generate long-term cash flows. Consequently, firms with higher IOS are more likely to improve their operating performance and profitability than firms with limited growth opportunities.

From a theoretical perspective, this finding supports Signaling Theory, which argues that investment decisions convey important information regarding a firm's future growth prospects. Firms that consistently undertake value-creating investments send positive signals to investors regarding management's confidence in future performance. These signals reduce information asymmetry between managers and investors, thereby strengthening market confidence and encouraging access to external financing required for business expansion. At the same time, the finding is also consistent with Agency Theory, which suggests that profitable investment opportunities reduce agency conflicts because managers are encouraged to allocate corporate resources toward projects that maximize shareholder wealth rather than pursuing unproductive investments.

The present finding is consistent with previous studies reporting that firms possessing greater investment opportunities generally achieve higher profitability because productive investments improve operational efficiency and revenue generation. However, several earlier studies conducted in manufacturing industries reported weaker or insignificant relationships. Such differences may arise because investment opportunities in manufacturing are often associated with shorter production cycles, whereas property and real estate investments require considerably longer development periods before generating revenue. The Indonesian property sector is characterized by long project completion horizons, substantial capital expenditures, and delayed cash inflows. Consequently, the economic benefits of investment decisions become more evident in long-term profitability rather than immediate financial performance.

The positive relationship between IOS and profitability

also has important managerial implications. Corporate managers should prioritize investment projects based on their long-term economic value instead of focusing exclusively on short-term accounting performance. Strategic land acquisition, project feasibility analysis, and effective capital allocation become essential managerial decisions because unsuccessful investments may lock substantial financial resources into unproductive assets. Therefore, investment planning should be integrated with corporate financial policies to ensure sustainable profitability and long-term competitiveness.

Dividend Payout and Profitability

The results demonstrate that Dividend Payout has a positive and significant influence on profitability, thereby supporting H4. Although dividend payments reduce retained earnings available for reinvestment, the findings suggest that firms distributing dividends generally exhibit stronger financial performance and greater earning capacity. Rather than weakening profitability, dividend distribution appears to reflect management's confidence in the firm's ability to maintain stable future earnings.

This finding is strongly supported by Signaling Theory, which proposes that dividend payments constitute credible signals regarding the firm's financial strength and future prospects. Because managers possess superior information about future cash flows, decisions to distribute dividends communicate positive expectations concerning future profitability. Investors therefore interpret stable dividend payments as evidence of sustainable corporate performance, leading to stronger market confidence and improved corporate reputation.

The finding also aligns with Agency Theory, which argues that dividend payments reduce agency conflicts between managers and shareholders by limiting the amount of free cash flow under managerial discretion. By distributing excess cash to shareholders, managers face greater discipline in allocating corporate resources efficiently, thereby improving operational performance and profitability.

The present result is generally consistent with previous empirical studies reporting positive associations between dividend policy and corporate profitability (Ovami & Nasution, 2020). Nevertheless, several previous studies have documented insignificant or even negative relationships, particularly in firms experiencing liquidity constraints. The difference may be attributed to the unique characteristics of Indonesia's property and real estate industry. Since property development projects require substantial external financing, only financially healthy firms possessing sufficient cash flows are capable of distributing dividends consistently. Consequently, dividend payments in this industry serve not only as a financing decision but also as an indicator of corporate financial strength.

From a managerial perspective, the findings suggest that dividend policy should not merely be viewed as a mechanism for distributing profits but also as a strategic communication tool. Managers should establish dividend policies that are consistent with long-term investment strategies while maintaining investor confidence. Stable dividend payments may strengthen market credibility without sacrificing future business expansion, provided that firms maintain adequate liquidity and investment capacity.

Profitability and Firm Value

The findings reveal that profitability has a positive and statistically significant effect on firm value, thereby supporting H5. This result indicates that firms generating higher returns on assets are more likely to achieve higher market valuations because investors perceive profitability as a reliable indicator of future financial performance and corporate sustainability. Higher profitability strengthens investors' expectations regarding future cash flows, leading to increased demand for

company shares and ultimately enhancing firm value.

This finding provides strong support for Signaling Theory, which emphasizes that profitability represents one of the most influential market signals available to investors. Since managers possess superior information regarding corporate performance, reported profitability serves as a credible signal concerning the firm's future prospects. Strong profitability reduces information asymmetry between managers and external investors, thereby increasing market confidence and improving firm valuation.

The result is also consistent with Agency Theory, which argues that profitability reflects effective managerial performance in utilizing corporate resources to maximize shareholder wealth. Higher profitability indicates efficient management of corporate assets and successful implementation of business strategies, thereby reducing concerns regarding managerial opportunism and agency costs.

The findings are consistent with numerous previous studies demonstrating that profitability positively influences firm value across various industries (Salsabilla & Rahmawati, 2021). However, the strength of the relationship appears particularly pronounced in Indonesia's property and real estate sector because investors frequently evaluate developers based on their ability to generate stable profits despite long project completion periods and cyclical market conditions. Given the substantial uncertainty associated with property investments, profitability becomes a critical indicator of project success and financial sustainability.

From a practical standpoint, managers should prioritize sustainable profitability rather than focusing solely on short-term revenue growth. Improving operational efficiency, optimizing project management, and strengthening financial performance are essential strategies for enhancing investor confidence and maximizing firm value over the long term.

The Moderating Role of Firm Size

The empirical results indicate that Firm Size significantly strengthens the positive relationship between profitability and firm value, thereby supporting H6. This finding suggests that profitability generates greater improvements in firm value among larger companies than among smaller firms. Larger firms generally possess broader asset bases, stronger financial capacity, greater market visibility, and better access to external financing, enabling investors to interpret profitability as a more credible signal of future corporate performance.

The moderating effect can be explained by both Signaling Theory and Agency Theory. From the perspective of Signaling Theory, profitability reported by large firms carries greater credibility because these companies are generally subject to stricter regulatory oversight, higher transparency requirements, and more comprehensive corporate governance mechanisms. Consequently, investors place greater confidence in profitability information disclosed by larger firms. Agency Theory further explains that larger firms tend to possess more sophisticated governance structures and stronger monitoring systems, reducing agency conflicts and increasing managerial accountability. As a result, improvements in profitability are translated more effectively into higher firm value.

The findings extend previous empirical studies by demonstrating that firm size should not merely be treated as a control variable but can function as an important moderating variable affecting the profitability-firm value relationship. While earlier studies generally examined firm size only as an independent determinant of firm value, the present study provides evidence that corporate size changes the strength of profitability's influence on market valuation (Pradanimas & Sucipto, 2022). This finding represents one of

the primary theoretical contributions of the study.

Within Indonesia's property and real estate industry, large firms generally possess diversified project portfolios, extensive land reserves, stronger banking relationships, and easier access to capital markets than smaller developers. These advantages enable profitable firms to capitalize more effectively on growth opportunities and sustain investor confidence, thereby strengthening the relationship between profitability and firm value.

From a managerial perspective, corporate managers should recognize that firm growth not only increases operational capacity but also enhances the market's response to improved profitability. Consequently, expansion strategies aimed at increasing total assets, strengthening corporate governance, and improving financial transparency may further enhance shareholder value.

Overall Theoretical Contribution

This study contributes to the corporate finance literature in several important ways. First, it integrates Trade-off Theory, Agency Theory, and Signaling Theory into a comprehensive framework explaining how financial distress, capital structure, investment opportunity set, and dividend policy influence profitability and subsequently affect firm value. Second, unlike many previous studies that treat firm size solely as a control variable, this research demonstrates that firm size functions as a significant moderator strengthening the relationship between profitability and firm value. Third, by focusing on Indonesia's property and real estate sector during 2010–2019, the study extends existing empirical evidence to a capital-intensive industry characterized by long investment horizons, substantial financing requirements, and cyclical business risks. These industry-specific characteristics provide additional insights into how corporate finance decisions influence financial performance and market valuation.

Managerial Implications

The findings provide several important managerial implications for corporate executives in the property and real estate sector. Managers should continuously monitor financial distress indicators to prevent financial deterioration that may reduce profitability. Capital structure decisions should be optimized by balancing debt financing and financial risk in accordance with Trade-off Theory. Investment decisions should prioritize projects capable of generating sustainable long-term returns, while dividend policies should be designed to maintain investor confidence without limiting future investment capacity. Furthermore, managers should recognize that corporate growth, measured through firm size, enhances the market valuation of profitable firms. Accordingly, expansion strategies should be accompanied by improvements in financial transparency, corporate governance, and operational efficiency to maximize shareholder value.

Policy Implications

The findings also have implications for regulators, investors, and policymakers. Financial regulators should encourage greater transparency in financial reporting and strengthen disclosure requirements related to corporate financial risk and investment activities, thereby reducing information asymmetry in capital markets. Investors may utilize financial distress indicators, profitability, and firm size as complementary criteria when evaluating investment opportunities within the property and real estate sector. Finally, policymakers should continue promoting financial market stability and long-term financing mechanisms that support sustainable development in capital-intensive industries, enabling property companies to undertake productive investments while maintaining healthy financial performance and enhancing firm value.

Conclusion

This study investigated the effects of financial distress, capital structure, investment opportunity set, and dividend payout on profitability, as well as the influence of profitability on firm value, while examining the moderating role of firm size in Indonesian property and real estate companies listed on the Indonesia Stock Exchange during the 2010–2019 period. The study contributes to corporate finance literature by integrating Trade-off Theory, Agency Theory, and Signaling Theory into a unified framework explaining how internal financial conditions influence corporate profitability and ultimately create firm value.

The empirical findings provide several important conclusions. First, financial distress has a significant negative effect on profitability, indicating that increasing financial pressure reduces firms' ability to generate returns from their assets. This finding emphasizes that maintaining financial stability is essential for sustaining operational performance in the capital-intensive property and real estate industry. Second, capital structure positively influences profitability, suggesting that an optimal combination of debt and equity financing enables firms to improve operational efficiency and benefit from productive leverage. Third, the investment opportunity set positively affects profitability, demonstrating that firms possessing stronger growth opportunities are more capable of generating sustainable earnings through productive investments. Fourth, dividend payout positively influences profitability, implying that stable dividend distributions serve not only as an indicator of financial strength but also as a mechanism for enhancing managerial discipline and investor confidence.

The study further demonstrates that profitability significantly increases firm value, confirming that firms with stronger financial performance receive higher market valuation because profitability functions as a credible signal of future corporate prospects. In addition, the findings reveal that firm size positively moderates the relationship between profitability and firm value. Larger firms strengthen the positive impact of profitability on market valuation because they generally possess greater financial resources, stronger corporate governance, wider access to external financing, and higher investor confidence. These findings indicate that firm size should be viewed not merely as a control variable but also as an important contextual factor influencing corporate value creation.

From a theoretical perspective, this study extends previous corporate finance research by demonstrating that the combined application of Trade-off Theory, Agency Theory, and Signaling Theory provides a more comprehensive explanation of value creation in capital-intensive industries. Moreover, unlike many previous studies that treated firm size only as an explanatory or control variable, this research demonstrates its significant moderating role in strengthening the profitability–firm value relationship. Consequently, the study provides additional empirical evidence that value creation is influenced not only by financial performance but also by firm characteristics that shape investors' perceptions of corporate quality.

The practical implications of this study differ across stakeholder groups. For corporate managers, priority should be given to maintaining financial stability by minimizing financial distress and optimizing capital structure, as these variables represent the fundamental drivers of sustainable profitability. Managers should also prioritize high-quality investment projects and adopt dividend policies that balance shareholder returns with future growth opportunities. For investors, profitability, financial distress indicators, and firm size should be jointly considered when evaluating investment decisions because these variables provide complementary

information regarding corporate performance and long-term value creation. For policymakers and capital market regulators, strengthening financial disclosure requirements and improving transparency regarding corporate financial conditions and investment activities may reduce information asymmetry and enhance market efficiency within the property and real estate sector.

Despite these contributions, several limitations should be acknowledged. First, the study focuses exclusively on property and real estate companies listed on the Indonesia Stock Exchange, thereby limiting the generalizability of the findings to other industries with different operational characteristics and financing structures. Second, the observation period covers 2010–2019, which does not capture the economic disruptions associated with the COVID-19 pandemic, the post-pandemic recovery period, or the recent changes in global interest rate policies that may substantially influence corporate financial behavior. Third, the study relies on specific measurement proxies, namely Altman Z-Score for financial distress, Debt-to-Equity Ratio (DER) for capital structure, CAPVA for investment opportunity set, Dividend Payout Ratio (DPR) for dividend policy, Return on Assets (ROA) for profitability, Price-to-Book Value (PBV) for firm value, and the natural logarithm of total assets for firm size. Although these measures are widely accepted in the literature, they may not fully capture all dimensions of the underlying constructs.

Future research should therefore extend this study in several directions. First, future studies should examine multiple industrial sectors to determine whether the observed relationships remain consistent across industries with different business characteristics. Second, researchers are encouraged to incorporate more recent observation periods, including the COVID-19 pandemic and post-pandemic years, to evaluate the stability of the proposed relationships under changing macroeconomic conditions. Third, future studies may employ alternative proxies, such as Tobin's Q for firm value, Return on Equity (ROE) for profitability, or other financial distress prediction models, to assess the robustness of the empirical findings. Finally, future research may expand the conceptual model by incorporating additional variables, including corporate governance, sustainability performance, environmental, social, and governance (ESG) practices, ownership structure, digital transformation, or macroeconomic factors, to develop a more comprehensive explanation of corporate value creation.

Overall, this study demonstrates that value creation in Indonesian property and real estate companies is fundamentally driven by sustainable profitability, which is shaped by sound financial management, productive investment decisions, appropriate financing policies, and strengthened by larger firm size. These findings contribute to a deeper understanding of how financial decision-making supports long-term corporate value creation in capital-intensive industries while providing practical guidance for managers, investors, and policymakers.

Author contributions

Meiliani Luckieta helped with the study's conception, research design, data collecting, data analysis, findings interpretation, and paper preparation. Along with approving the final version of the article for publication, the author was also in charge of critically examining and editing the work for significant intellectual content. Siti Nur Aisyah assisted in finalizing the manuscript and checking its completeness and consistency prior to submission.

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