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## THE ROLE OF PROFITABILITY IN MEDIATING THE EFFECT OF LEVERAGE ON FIRM VALUE AT PT INDOFARMA TBK

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### Abstract

The purpose of this study is to investigate how much profitability can mediate the connection between firm value and leverage at PT Indofarma Tbk between 2019 and 2023. The route analysis method was utilized in this study's quantitative methodology, and SPSS version 22 software was used for data processing. The annual study's companies' financial statements period served as the data source. With a coefficient value of -3.251 and a significance level of  $p = 0.000$ , the findings of the analysis show that leverage significantly reduces firm value; however, no real impact of leverage on profitability was found (coefficient = 0.000;  $p = 0.904$ ). On the other hand, the findings demonstrates that profitability raises the worth of the company, but this relationship is not statistically significant (coefficient = 19.125;  $p = 0.288$ ). These results indicate that how leverage and corporate value are related is not significantly mediated by profitability. In terms of theory, this study confirms that capital structure, especially in the form of leverage, has a direct impact on firm value without involving profitability as an intermediary channel. The practical implication of this result is the importance of controlling the debt structure so as not to cause a decrease in firm value, as well as the need for management to remain focused on improving the efficiency of asset performance. This study expands academic understanding of the dynamics between leverage, profitability, and firm value, and provides strategic insights for decision makers, especially in terms of optimal capital structure management.

**Keywords:** Profitability, Leverage, Firm Value, Debt to Equity Ratio, Return on Assets, Price to Book Value

## INTRODUCTION

In recent years, to be precise, in 2019, the entire country has been rocked by the COVID-19 outbreak. The effects are numerous, one of which is the global economy slowing down. In 2019, Indonesia experienced Indonesia's COVID-19 epidemic with the discovery of the first case. The deterioration of national economic performance is influenced by this circumstance (IMF, 2020) The IMF predicts world economic growth of 3.3%, surpassing the 2.9% recorded in 2019. However, this projection is still potentially affected by factors such as productivity declines, protectionist policies, and trade wars. (Kementrian Keuangan Republik Indonesia, 2020).

Global economic growth has been significantly affected by the COVID-19 epidemic, as reflected in the data for the first quarter of 2020. China, which became the first country to face the virus, experienced a 6.8% quarterly economic contraction, the worst figure since 1976. Nonetheless, China managed to recover quickly and maintained positive growth throughout 2020. (CNN Indonesia, 2020). In the second quarter of 2020, economic conditions reached their lowest point throughout the pandemic. Many countries were unable to avoid recession, which was reflected in the negative economic growth for two consecutive quarters experienced by several countries, places including Mexico, the Philippines, Singapore, Hong Kong, and Europe. (Kementrian Keuangan Republik Indonesia, 2020).

A high firm value generally corresponds to an increase in the market price of shares, and this is a desirable target for investors. When a decline in the company's value occurs, the effect will be felt on evaluating the efficiency of the business, and risks reducing the amount of profit earned by shareholders (Lamba & Atahau, 2022). Investment decision-making by investors requires analysis of companies that show superior performance and have high value (Sugosha, 2020). Successful investors are those who are able to utilize information from financial statements to analyze the market and choose the right investment to make a profit (Astuty, 2017).

One of the significant suppliers of healthcare goods in Indonesia is the pharmaceutical company PT Indofarma Tbk (INAF). Ironically, the firm's financial outcomes over the past few years have been unfavorable. One of the key markers of sustainability and operational health in the business sector is the firm's financial outcomes. As an important part of Indonesia's pharmaceutical sector, PT Indofarma Tbk has faced significant challenges in recent years, mainly associated with financial and company-related issues value issues faced by the pharmaceutical sector. Changes in the share price of PT Indofarma Tbk in 2019 and 2023 reflect market dynamics and investor sentiment towards the company in Figure 1:

**Figure 1.**

### Diagram of Share Price of PT Indofarma Tbk Period 2019-2023



Source: (IDN Financial, 2025)

View stock price information in Table 1, 2019 PT Indofarma Tbk share price started the period with a high value, 6,000, then experienced a gradual decline until it reached its lowest point at 500 at the year's conclusion. 2020 the share price showed an upward trend from the beginning of the year, peaking above 3,500 in the middle of the year, before declining again until the end of the year. 2021 the share price fluctuates around 2,000-2,500, showing no clear trend. 2022 the share price experiences a gradual decline until the end of the year, hovering around 1,000. 2023 the share price continued to decline, hovering below 1,000 to a low of around 580 at the end of the period. Overall, the share price of Pt Indofarma Tbk showed a long-term downward trend over the 2019-2023 period (IDN Financial, 2025).

The profit generated by PT Indofarma has also decreased and even reached a loss. The financial performance of PT Indofarma Tbk in the last 5 years 2019-2023 reflects the challenges faced by the company in table 1:

**Table 1.**  
**Company Net Profit Financial Statements**  
**PT Indofarma Period 2019-2023 (in rupiah)**

Year	Net Profit
2019	7.961.966.026
2020	30.020.709
2021	(37.571.241.226)
2022	(457.649.309.385)
2023	(721.000.075.536)

Source: Data processed (www.idx.co.id)

Through the information in Table 1 shows that PT Indofarma Tbk experienced variations or inconsistencies in its movements, in terms of net profit during the period 2019 to 2023. In 2019, the company recorded a net profit of IDR 7.96 billion. However, from 2021 to 2023, the company experienced worsening losses, with net profit in 2020 recorded at IDR 30.02 billion and deepening in 2021 with a loss of IDR -37.57 billion. In 2022, the loss got bigger with a value of IDR -457.64 billion, and in 2023 the company recorded a loss of IDR -721.00 billion (Data Diolah Dari Laporan Keuangan PT Indofarma Tbk, 2025).

One of the internal factors that is crucial in assessing a company's worth is leverage. Leverage demonstrates the size of the debt component of the company's capital structure, which indicates the degree of financial risk and the effective utilisation of outside funding (Nailufar, 2025). A number of studies show that leverage plays a significant role in influencing firm value, both positively and negatively. (Kartika Dewi & Abundanti, 2019) discovered that effectively managed leverage helps to boost business value and establish investor trust. On the contrary, (Putri & Hendriyani, n.d.) found that optimally managed leverage has the potential to foster investor confidence while strengthening the fundamental value of the company. In contrast, research (Isnaini Puspitasari et al., n.d.) suggests that a high degree of leverage may reduce the value of the company by raising the danger of insolvency.

This discrepancy in results suggests that earlier studies on the impact of leverage on business value were inconsistent. In an effort to explain these inconsistencies, some researchers began to include mediating variables, such as profitability, to better understand

the causal relationship. Because profitability demonstrates operational effectiveness in managing resources and obligations, it is thought to mitigate the impact of leverage on company value (Yulimtinan et al., 2021). However, a recent study by (Evelyne et al., 2024a) still shows that the mediating role of profitability is not fully conclusive, still has a dependence on industry characteristics and company conditions. Thus, further research is needed to explore this relationship in more depth, especially in companies with high financial stress such as PT Indofarma Tbk in the post-pandemic period.

Therefore, in order to fulfil shareholder expectations, be competitive in the market, and ensure the sustainability of their operations, businesses must maintain and increase their profitability. A thorough grasp of the link between the variables in issue will be provided by this study's examination of several factors that may have an impact on profitability, including firm value and leverage (Nugroho & Pristiana, 2021).

This study uses profitability as a mediating variable as it may indirectly affect corporate value. Profitability is a measure of a company's capacity to earn a profit, and it can positively impact changes in the share price (Kartika & Kelana, 2020a). The capacity of a business to generate a profit from its activities is referred to as profitability (Kusuma et al. 2021). According to signalling theory, high profitability denotes bright business prospects that may draw in investors and raise demand for the company's stock. The positive correlation between business value and profitability suggests that a rise in firm value will coincide with a rise in profit (Yulimtinan & Atiningsih, 2021)

The results of earlier studies on the connection between leverage and business value have been mixed, with some seeing a positive impact and others finding no discernible association. This inconsistency raises the question of whether other variables bridge the relationship. One potential variable is profitability, which reflects a firm's operational efficiency in managing its capital structure. However, empirical findings on the mediating role of profitability have also not been fully conclusive, especially in the context of the pharmaceutical sector affected by the pandemic. With a case study on PT Indofarma Tbk during 2019-2023, this study attempts to close this gap by evaluating the impact of leverage on firm value, both directly and indirectly through profitability.

## **REVIEW OF LITERATURE**

### **Signaling Theory**

According to the signalling theory, businesses can educate the market by presenting financial statements and strategy choices that outline anticipated future performance (Brigham, 2020). In this instance, investors view a high degree of profitability as a favourable sign, which might raise the market's assessment of the company's worth. Meanwhile, a company's capital structure, including its level of leverage, can also indicate how risky or stable it is. Investors will have a positive perception of the company's performance if it can effectively manage debt while still demonstrating improved profit performance (Kartika & Kelana, 2020b). Therefore, the idea that profitability and leverage may have a direct or indirect impact on company value is supported by signalling theory.

### **Profitability**

Recent empirical research indicates that ROA, a measure of profitability, is not only a performance indicator but also a crucial link in bridging the gap between company value

and leverage. (Ichsan et al., n.d.) discovered that ROA fully mediates the effect of leverage on firm value. This conclusion is supported by studies showing that profitability also increases the effect of leverage on stock returns (Chauhan, 2024). On the other hand, a study in the healthcare sector by (Pelita Adisty & Gusti Ketut Agung Ulupui, 2024) shows that the mediation of profitability is partial and depends on the industry context. Meanwhile, (Evelyn et al., 2024b) prove that leverage through profitability can raise the company's worth, especially companies in the industrial sector. In accordance with these findings, this study determines ROA as a mediating variable in the theoretical model developed to examine whether profitability helps bridge the influence of leverage on firm value at PT Indofarma Tbk.

### **Leverage**

Leverage indicates how much a business relies on loans from outside sources for funding. Corporations or companies will be required to bear greater financial risks as debt increases. However, if leverage is effectively applied to profitable initiatives, it may also be a tool to raise the company's worth (Yohanson & Putra, 2020). (Hermuningsih et al., 2022; Nugroho & Pristiana, 2021) shows that leverage impacts through financial distress and profitability to ultimately affect firm value. Instead, (Saputra et al., 2024) discovered that leverage increased company value in the plantation industry, despite profitability having the reverse impact. A study in the property sector by (Fadhilah & Widajantie, 2024) strengthens the finding of significant positive leverage on value, without profitability mediation. In other words, depending on the financial situation and industrial setting, the empirical findings regarding the link between leverage and business value have not been consistent.

### **Firm Value**

Firm value is generally represented through the PBV ratio, which describes the market's assessment of the company's net worth. Research on the F&B sector on the IDX by (Oktaviani et al., 2024) discovered that PBV is significantly positively impacted by profitability and leverage, suggesting that capital optimization and profitability have an important role in strengthening firm value. On the contrary, (Gultom et al., n.d.) reported that while profitability increases PBV, leverage has a negative impact, suggesting that an excessive proportion of debt may reduce investor attractiveness. (Markonah et al., 2020) also reinforces the finding that profitability and leverage are equally important in determining firm value in the manufacturing sector, with ROA showing a dominant influence.

### **Hypothesis**

#### **Effect of Leverage on Profitability**

The use of debt might be seen as a sign that the business is confident in its ability to turn a profit from outside funding, according to signalling theory (Brigham, 2020). Optimal leverage management is believed to be able to encourage increased profitability through the expansion of working capital and investment capacity. (Sutama & Lisa, n.d.). According to (Yulimtinan & Atiningsih, 2021) and (Sihombing & Astuty, n.d.) leverage significantly increases the level of profitability. (Isnaini Puspitasari et al., n.d.) assert that leverage has no discernible impact on the degree of firm success in the real estate sector.

**H<sub>1</sub>: Leverage has a positive and significant effect on profitability**

#### **The Effect of Leverage on Firm Value**

According to the trade-off theory, debt may boost firm value through tax efficiency as long as it is used within optimal bounds (Ai et al., 2020). According to a study by (Bui et

al., 2023), in Vietnam, leverage has a considerable and beneficial impact on business value. Conversely, a study on the manufacturing sector on the IDX (Pratami & Munashiroh, 2024) found no discernible relationship between leverage and company value.

**H<sub>2</sub> : Leverage has a positive and significant effect on firm value.**

#### **The Role of Profitability on Firm Value**

According to signalling theory, investors view a high degree of profitability as an indication of the company's operational effectiveness and long-term viability (Brigham, 2020). Study by (Setiawanta & Hakim, 2020), the substantial impact of ROA on company value in the banking sector. However, a study conducted in the real estate industry (Khalifaturofi'ah & Setiawan, 2025) found no evidence of a substantial impact of profitability testing on company value. Additional empirical testing is supported by the difference in outcomes.

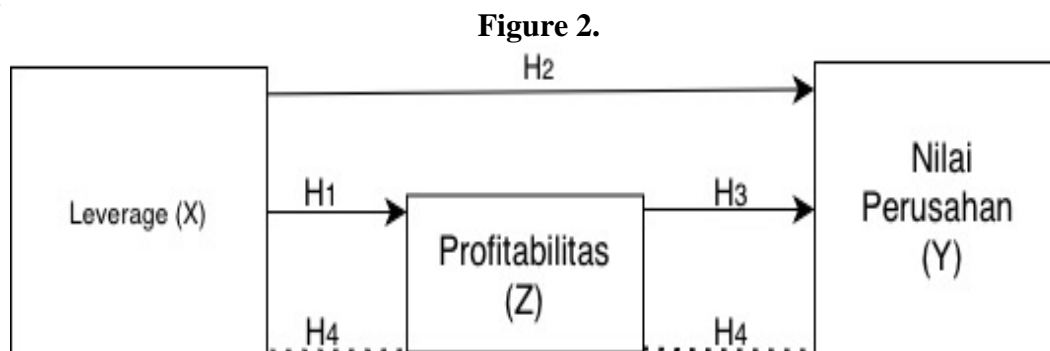
**H<sub>3</sub>: Profitability has a positive and significant effect on firm value**

#### **The role of Profitability mediates the effect of Leverage on Firm Value**

Profitability may act as a moderator in the link between leverage and firm value as, in accordance with signalling theory, investors see a company's capacity to generate profits through the use of debt favourably (Kartika & Kelana, 2020a). According to a study by (Evelyne et al., 2024a), the impact of leverage on business value is mediated by profitability. (Permatasari & Maryanti, 2024) did not find significant mediation because leverage has not been shown to affect profitability or firm value directly.

**H<sub>4</sub> : Profitability mediates the effect of leverage on firm value**

#### **Hypothesis Framework**



Source: Processed by researchers 2025

#### **RESEARCH METHOD**

This study is a component of a larger body of quantitative research that investigates the causal link between business value, profitability, and leverage using the causal associative approach. This approach uses profitability as a mediating variable to ascertain the degree to which leverage directly or indirectly impacts business value (Sugiyono, 2017).

The focus of this research is PT Indofarma Tbk, a business that is listed on the Indonesia Stock Exchange (IDX). This study will last for five years, from 2019 to 2023. This company was chosen because there was a significant decline in profitability and company value during this period. The secondary quantitative data of this study comes from the annual

financial statements of PT Indofarma Tbk, which is shown on the company's official website. and IDN Financial's IDX page (2025) and the company's official website. (Data Diolah Dari Laporan Keuangan PT Indofarma Tbk, 2025).

There are three variables used in this study, namely: Leverage (X): measured by Debt to Equity Ratio (DER) Profitability (Z): measured by Return on Assets (ROA) Firm Value (Y): measured by Price to Book Value (PBV).

**Table 2.**  
**Variable Operationalization**

Variable	Indicator	Measurement	Scale
Firm Value (Y)	<b>Market Price per Share Book Value per Share</b>	<b>PBV = Market Price per Share Book Value per Share</b>	<b>PBV</b>
Leverage (X)	<b>Total Debt Total Equity</b>	<b>DER = Total Debt X 100% Total Equity</b>	<b>DER</b>
Profitability (Z)	<b>Net Profit Total Asset</b>	<b>ROA = Net Profit X 100% Total Assets</b>	<b>ROA</b>

Source: Processed by researchers 2025

The data was analysed using analytical mediation analysis, which aims to determine if profitability can lessen the effect of leverage on business value. The following procedure was used to carry out the phases of the analysis in accordance with the approach (Baron & Kenny, 1986): This study's objectives are to examine the direct effects of leverage on company value, evaluate the impact of leverage on profitability, and look into the connection between firm value and profitability. A study was also carried out to see if profitability acts as a mediator between leverage and business value. The data analysis process was conducted using SPSS version 22 software. Before the route analysis test, traditional assumption tests were used, including as testing for autocorrelation, heteroscedasticity, multicollinearity, and normality. However, this study did not conduct robustness tests such as sensitivity analysis of the model or estimation results. This is due to the limited scope of data that only comes from one company with a limited number of observations, making it impossible to conduct sensitivity testing adequately.

Additionally, the study's sample size is restricted to PT Indofarma Tbk, a single firm, and its five years of observation from 2019 to 2023. The external validity of the analytical model and the extent to which the research findings are broadly applicable may be affected by this small sample size. Therefore, interpretation of the results should be done with caution and not broadly generalized to the entire pharmaceutical industry sector.

## RESULTS AND DISCUSSION

This study's goal is to assess, using predefined sample criteria and profitability as a mediating variable, the degree to which leverage impacts business value. To ensure that the data used meets the conditions of optimality, linearity, and independence from bias, the first step in the analysis is to evaluate the classical assumptions. The data is initially examined using many traditional assumptions, such as checks for autocorrelation, heteroscedasticity,

multicollinearity, and normality, before regression analysis is performed. The table below displays the test results:

**Table 3.**  
**Classical Assumption Test Results**

Test Type	Test Results	Criteria	Conclusion
<b>Normality Test</b> • <b>Kolmogrov smirnov</b>	Kolmogrov Smirnov Value 0,180	>0,05	Passed Normality Test
<b>Multikolinearity Test</b>	Tolerance Value of DER 0,994 and VIF Value of DER 1,006 Tolerance Value of ROA 0,994 and VIF Value of ROA 1,006	Tolerance Value: >0,05 VIF Value: <10	Passed Multikolinearity Test
<b>Heteroscedasticity</b> • <b>Glejser</b>	Significance Value of DER 1,000 Significance Value of ROA 1,000	Significance Value >0,05	Passed Heteroscedasticity Test
<b>Autocorrelation Test</b> • <b>Durbin Waston</b>	DU Value = 1,5 DW Value = 2,330 4-DU Value = 2,5 1,5<2,330<2,5	DU<DW<4-DU	Passed Autocorrelation Test

Source: (Data Processed From Income Statements of PT Indofarma Tbk, 2025) and Data output SPSS (22) 2025

A significant value of 0.180 was obtained using the Kolmogorov-Smirnov approach for normality testing, which is more than the 0.05 limit. This suggests that the data set is regularly distributed. The multicollinearity test revealed that all independent variables satisfied the criteria, demonstrating the lack of multicollinearity, with a tolerance value of 0.05 and a VIF less than 10. Furthermore, a significant value above 0.05 is obtained from the Glejser method heteroscedasticity test, suggesting that the data does not exhibit any signs of heteroscedasticity. Additionally, the Durbin-Watson autocorrelation test produces DW values that fall within the range that shows the model has no autocorrelation.

**Path Analysis Test Results**

**Table 4.**  
**Regression 1: Effect of X on Y**

Model	Unstandardized Coefficients			Standardized Coefficients		
		<b>B</b>	<b>Std.Error</b>	<b>Beta</b>	<b>t</b>	<b>Sig</b>
	Constant	1772,526	640,632		2,767	0,070
	Leverage	-3,251	0,080	-0,999	-40,588	0,000

a. Dependent variable: **Firm Value**

Source: Data Output SPSS (22) 2025

$$Y = \beta_0 + \beta_1 X + \varepsilon$$

Regression 1 (X → Y), Koefisien (c) = -3,251, Sig = 0,000 (< 0,05)

**Interpretation:**

Leverage and firm value are negatively correlated, as seen from the negative coefficient value of -3.251. Stated otherwise, a one-unit rise in leverage will lead to a 3.251-unit drop in firm value, assuming all other parameters stay the same. According to the trade-off argument, a company's financial burden may rise as a result of excessive debt use, which might ultimately lower the firm's value. This result makes sense in the case of PT Indofarma Tbk, which experienced a downward trend from 2019 to 2023 as the company's large debt burden was not supported by adequate profit-generating capacity. This result also confirms the study findings (Gultom et al., n.d.), which indicate that excessive leverage actually decreases investor attractiveness and decreases business value.

The p-value (Sig) = 0.000, which is smaller than 0.05, indicates that the effect of leverage and firm value is statistically significant.

**Conclusion: Leverage has a negative and significant effect on Firm Value**

**Table 5.**  
**Regression 2: X Effect on Z**

Model	Unstandardized Coefficients			Standardized Coefficients		
		B	Std.Error	Beta	t	Sig
	Constant	-23,934	23,861		-1,003	0,390
	Leverage	0,000	0,003	-0,075	-0,131	0,904

a. Dependent variable: **Profitability**

Source: Data Output SPSS (22) 2025

$$Z = \beta_0 + \beta_1 X + \varepsilon$$

Regression 2 (X → Z), Koefisien (a) = 0,000, Sig = 0,904 (> 0,05)

**Interpretation:**

Coefficient (a) = Leverage has no impact on profitability, as indicated by the coefficient value of 0.000. In other words, the dependent variable is unaffected by changes in the independent variable. Additionally, the significance value (p-value) of 0.904, which is greater than the 0.05 limit, shows that the effect of leverage on profitability is not statistically significant. This result runs counter to the signalling theory, which holds that a company's optimal use of debt can provide investors with a reliable indicator of the firm's potential for profit (Brigham, 2020). However, in the case of PT Indofarma Tbk, debt is not used optimally to generate profits, as shown by the low ROA value during the observation period. This confirms that the industry context, as well as the company's internal management, play an important role in determining whether leverage will have an impact on profitability. This study confirms the findings of studies by (Isnaini Puspitasari et al., n.d.) which found no relationship between profitability in some industries and leverage.

**Conclusion: Leverage has no significant effect on Profitability**

**Table 6.**  
**Regression 3: The Effect of X and Z on Y**

Model	Unstandardized Coefficients			Standardized Coefficients		
		B	Std.Error	Beta	t	Sig
	Constant	2230,442	636,395		3,505	0,073
	Leverage	19,125	13,324	0,30	1,435	0,288

	Profitabilitas	-3,244	0,069	-0,997	-46,978	0,000
a. Dependent variable: <b>Firm Value</b>						

Source: Data Output SPSS (22) 2025

$$Y = \beta_0 + \beta_1 X + \beta_2 Z + \varepsilon$$

Regression 3 (X & Z → Y), Coefficient (b) = 19.125, Sig = 0.288 (> 0.05), Coefficient (c') = -3.244 (smaller than the previous c), Sig (X → Y after inserting Z) = 0.000

**Interpretation:**

Coefficient (b) = Firm value is positively impacted by profitability, as indicated by the coefficient value of 19.125. The p-value of 0.288, which is more than the significance level of 0.05, however, indicates that the influence is not statistically significant. However, signalling theory, which holds that profitability is a good indicator for investors, is supported by the coefficient's positive direction (Brigham, 2020). This finding shows that the value of PT Indofarma Tbk is not significantly affected by profitability. Based on the ROA data in the 2019-2023 financial statements, the low level of profitability throughout the observation period is likely to be the cause of this condition.

The coefficient (c) = -3.244 illustrates how leverage affects firm value once profitability is factored into the model. After accounting for profitability, the direct impact of leverage on firm value is lessened, as indicated by the fact that c is lower than it was previously. With a p-value of 0.000, the value of c is still significant, indicating that leverage has a large but diminished impact on company value. This indicates that profitability does not mediate the relationship effectively. In the framework of (Baron & Kenny, 1986), The mediation condition is not met because the effect of Z on Y is not significant. Therefore, in this model, profitability does not play a significant mediating role, and leverage continues to be the main driver of firm value..

**Conclusion:**

There is no significant mediation from profitability, because the p-value of b (Z → Y) > 0.05 leverage still has a significant effect on firm value although the effect is smaller after including profitability, the mediation effect does not exist because profitability does not have a significant effect on firm value.

**General Conclusion:**

In this model, profitability cannot be regarded as mediating the relationship between leverage and firm value because it has no real impact on the latter. Nevertheless, leverage still has a significant impact on firm value, albeit a smaller one when profitability is taken into account, indicating partial mediation or residual direct influence.

**Leverage has a negative and significant effect on Firm Value**

The results of the first hypothesis test show that the leverage variable has a regression coefficient of -3.251 and a p-value of 0.000, both of which are below the significance level of 0.05. This finding suggests that leverage significantly reduces the value of a company. The negative coefficient value means that a one-unit increase in leverage will lead to a 3.251-unit drop in firm value if all other parameters stay the same.

Leverage in this sense refers to how a business uses debt to fund operations or investments. An increase in leverage reflects the company's increasing dependence on debt financing to run its operations. A high level of leverage has the potential to increase risk, especially if the company fails to manage its debt obligations effectively. Investors are

usually more cautious of companies with a large debt structure, as interest expense and other payment obligations can put pressure on the company's financial condition. Consequently, companies with high leverage are often perceived as having greater risk, which can reduce investor interest and have an impact on reducing firm value. This research is in line with the research results (Christiani et al., 2019), (Yulimtinan & Atiningsih, 2021) that leverage has no effect on firm value.

The signaling theory perspective, which states that a firm's capital structure may signal to the market regarding the firm's internal problems, is actually supported by these findings, although the data show a large negative effect. High leverage that is not matched by adequate earnings performance is considered a negative signal by investors as it indicates high financial risk and potential default. Therefore, the decline in firm value in this context reflects the market's rational reaction to the bad signal from the debt structure of PT Indofarma Tbk.

#### Leverage has no significant effect on Profitability

According to the findings of the second hypothesis test, the leverage variable has a regression coefficient of 0.000 and a significance value (Sig) of 0.904. Since leverage's significance value exceeds the 0.05 cutoff, it may be said to have no discernible effect on profitability. The regression coefficient value ( $B = 0.000$ ) further suggests that a one-unit increase in leverage has no discernible effect on profitability because the value is so near to zero.

Leverage and profitability do not affect each other statistically significantly, based on the Sig value of 0.904 ( $>0.05$ ). In other words, a change in leverage has no noticeable effect on the company's profitability. Good financial management can ensure that even if a company has a certain level of debt leverage, its impact on profitability can be minimized through appropriate operational efficiency and investment strategies. If the firm has access to low-interest loans or has an effective debt management strategy, an increase in leverage may not be too burdensome to the firm's profitability. The findings of this study support previous research conducted by (Atiningsih et al., n.d.) and (Simanjuntak et al., 2023). This shows that the value of the firm is not too influenced by the amount of leverage it has.

Theoretically, this condition shows that leverage signals are not able to be translated into strong earnings performance, which indicates the weakness of leverage effectiveness in creating added value in this company. In the context of signaling theory, the absence of leverage effect on profitability reflects the company's failure to convert external financing into positive signals through operational performance. This finding supports the study of (Isnaini Puspitasari et al., n.d.), which shows that the relationship between leverage and profitability is strongly influenced by the efficiency in managing funds and the cost structure in the related industry sector.

#### **Profitability has a positive effect on Firm Value**

Because the test findings demonstrate that profitability significantly and favourably affects business value, the third hypothesis is accepted. This is supported by the profitability regression coefficient of 0.288 with a significance value of 0.000, which is far below the 0.05 cutoff. Consequently, it can be said that a rise in profitability will greatly boost business value, with a rise in profitability causing a rise in firm value and vice versa.

The ability of a business to make money from its capital is called profitability. The attractiveness of a company as an investment object increases with its level of profitability

because investors will get greater rewards. This result is consistent with the signaling hypothesis, which states that higher profitability gives investors hope for the future of the company. Higher future profits have the ability to increase investor confidence in the company's shares, which raises the share price and increases the value of the company. The findings of this study corroborate the findings of (Chabachib et al., 2019), which found that profitability significantly and positively affects firm value.

However, it should be noted that despite the positive direction of the coefficient, in this regression result, the significance of profitability does not fulfill the mediation condition. This could be due to the inconsistent fluctuations in PT Indofarma's profit performance, as reflected in the company's financial data during 2019-2023, which shows a trend of consecutive losses. Thus, while profitability generally signals good news, the historical context and company-specific performance still determine the strength of the signal.

### **Profitability does not mediate the effect of Leverage on Firm Value**

Firm value is not significantly affected by profitability, as indicated by the significance value of 0.288 ( $p > 0.05$ ). Furthermore, the impact of leverage is still considerable with a p-value of 0.000, although the coefficient of leverage on firm value drops slightly (from -3.251 to -3.244) after profitability is included in the model. This shows that profitability is not a mediating factor in the link between leverage and firm value. The research (Eka Putri et al., 2021) is supported by the findings of this investigation.

In the signaling theory framework, this result indicates that leverage as a negative signal remains dominant in influencing market perception of firm value, and profitability is not strong enough to obscure or offset this influence. The non-fulfillment of one of the mediation conditions, namely the significance of the effect of profitability on firm value, makes it clear that the debt structure at PT Indofarma has not been able to translate into profit performance that increases market attractiveness. This is in line with the company's financial condition, which consistently shows negative results, making the positive signal from profitability invalid in the eyes of investors.

## **CONCLUSION**

The research findings support the conclusion that leverage significantly and negatively affects firm value. This shows how firm value tends to decrease as leverage increases. Businesses with high levels of leverage are usually seen as riskier and less attractive to investors, which lowers firm value. Furthermore, leverage does not have a clear impact on profitability, which suggests that the amount of debt held by a firm does not necessarily result in the amount of profit earned. This outcome is probably influenced by additional elements, including financial management practices and operational effectiveness. Nonetheless, there exists a positive correlation between firm value and profitability; the greater the profitability, the higher the business value. These findings imply that profitability is crucial for drawing in investors and fostering the expansion of a company's worth. However, even if profitability is a part of the model, leverage still has a significant influence on firm value; hence, profitability does not mediate the link between leverage and firm value.

Based on these findings, the management of PT Indofarma Tbk is advised to be more careful in managing debt, namely by paying attention to the ideal leverage ratio in order to minimize the possibility of a decrease in company value. In order for debt financing to truly

boost profitability in real terms, a thorough assessment of operational effectiveness and profitable investment is also required. However, before making an investment, investors should consider the leverage ratio and profit performance, as the results indicate that an excessively debt-dependent capital structure may be a warning flag in the capital market. Company policy should be directed at increasing Return on Assets (ROA) through asset optimization and sustainable product innovation, given the role of profitability in shaping market perceptions of company value. The government or capital market authorities can also consider providing ideal leverage guidelines based on industry sectors, especially in the fluctuating post-pandemic economic conditions. Therefore, this study shows that leverage affects business value directly, independent of profitability. To prevent an adverse impact on firm value, businesses should manage their capital structure carefully and refrain from using excessive amounts of leverage. Furthermore, increasing profitability is still important to attract investors and increase firm value.

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