International Journal of Business and Management Invention (IJBMI)
ISSN (Online): 2319 – 8028, ISSN (Print): 2319 – 801X
www.ijbmi.org || Volume 8 Issue 02 Series. I || February 2019 || PP 49-55

The Influence of Financial Leverage toward Profitability Through Business Risk As Intervening Variables In LQ45 Companies Listed In Indonesia Stock Exchange (2013-2017)

Punandra Cahya N.S

Punandra Cahya N.S, Post Graduate Student, Malangkucecwara School of Economics, Malang, Indonesia.

ABSTRACT: The purpose of this research is to analyze the influence of leverage (DER) toward profitability (ROA) and business risk (BEP) as intervening variabel. The sample used in this research by purposive sampling method based on the existing criteria in 27 companies were selected as research samples during the period 2013 - 2017. Hypothesis testing was carried out using the Partial Least Square (PLS) method.

The result of hypothesis testing found that: 1). leverage influence negatively toward profitability; 2). Leverage influence positively toward business risk; 3). Business risk influence positively toward profitability. The results of the goodness of fit (Q-square) test show that the magnitude of the diversity of research data is 99.8% and the remaining 0.2% is influenced by other variables outside the model.

KEYWORDS: Leverage, Business Risk and Profitability

Date of Submission: 24-01-2019 Date of acceptance: 08-02-2019

I. INTRODUCTION

The company is certainly not only required to produce good quality products, but also must be able to manage its finances well, it is meaning that policies in financial management must ensure the sustainability of the company's business effected the company's objectives can be achieved (Furaida, 2010). One of the goals of a company is to earn profit which reasonable for shareholders. The company's profits based on the level of profitability in the company. Profitability is a ratio to assess a company's ability to achieve a profit (Kasmir, 2012). If the company cannot fulfill the objectives then the company will cannot develop, survive and be socially responsible.

There are many variables can influence of profitability such us leverage and business risk. Profitability is the net final results from various policies and decision (Weston, 1999). Leverage is a ratio that measures how much the company is financed with debt. It describes the relationship between corporate debt to capital, this ratio can measure how far the company is financed by debt or outside parties with the ability of the company described by capital (Harahap, 2013). Leverage Ratio is measuring how much the company is financed with debt (Fahmi, 2013). In business development, the company should face obstacles and difficulties both small and big obstacles. These constraints and difficulties are commonly known as business risks. Business risk is uncertainty that possible give rise to losses (Salim, H. Abbas, 2007). In addition, gaining the profits in the business, companies should prepare to face business risks. In the fact, even companies have been successful they still face business risks because business risk involved a part of a company.

Companies listed on LQ45 means that large companies which also should face significant risks, including the risk of inflation and changes in exchange rates, the risk of decreasing customer desires for the products produced, the risk of difficulty in raw material production, the risk of disharmony with creditors which can inhibit the addition of capital obtained from creditors, the risk of competition in the business world is getting tighter and the risk of global economic conditions. If the company faces these risks, the company will fail to generate profits in running the company's operations and the company will also face the risk of business bankruptcy (Furaida, 2010). In a company, business risk will increase if subject use a high debt strategy. This will also increase the probability of bankruptcy. The results show that companies with high risk should use less debt to avoid the possibility of bankruptcy (Puspida, 2013).

Based on the above background, the formulation of the problem in this study is (1) How is the leverage influence toward profitability on LQ45 companies listed in the Indonesia Stock Exchange? (2) How is the leverage influence toward business risk in the LQ45 company listed on the Indonesia Stock Exchange? (3) What is the influence of business risk toward profitability on LQ45 companies listed in the Indonesia Stock Exchange?

II. THEORETICAL FRAMEWORK AND HYPOTHESIS DEVELOPMENT

Profitability

Profitability is the ratio to assess the company's ability to achieve a profit (Kasmir, 2012). According to Weston (1999), profitability is the net final results from various policies and decision. This profitability provides an illustration of how effective the company operates effected to provide benefits for the company’s wealth or assets owned to generate corporate profits (operating assets). In the company's operations, profit is an important element in ensuring the continuity of the company with the ability to make a profit by using all the company's resources, the company's goals will be achieved.

Profit is the result of income from sales which is reduced by expenses. Profitability is the company's ability to obtain profits related to the total assets, sales and own capital, thus profitability analysis is very important for long-term investors because with the profitability analysis shareholders will see how much profit will be obtained in the form of dividends (Munawir, 2010).

Profitability in this research is measured by Return on Assets (ROA). Return on Assets (ROA) which is the ability of the capital invested in all assets to generate profits for all investors (bond holders and shares). Return On Assets (ROA) is a ratio that shows results (return) on the amount of assets used in a company (Kasmir, 2012). Return On Assets (ROA) is often also referred to as Return On Investment (ROI) because this ROA looks at the extent to which investments that have been invested are able to provide returns as expected and the investment is actually the same as the company's assets invested or placed.

Leverage

Leverage ratio is a ratio that measures how much a company is financed with debt. Leverage is the ratio that describes the relationship between corporate debt to capital, this ratio can see how far the company is financed by debt or outside parties with the ability of the company described by capital (Harahap, 2013). Leverage Ratio is a measure of how much a company is financed with debt (Fahmi, 2013). This research is measured by Debt to Equity Ratio (DER). This ratio is used to compare sources of capital derived from debt (long-term debt and short-term debt) with own capital. This is usually used to measure the financial leverage of a company (Sartono, 2010). The higher debt to equity ratio means the companies have much loaned fund to finance their assets, on the contrary the lower the ratio, most of the asset financed by the itself fund (Bangun, 1989).

Business Risk

Business risk is uncertainty regarding the projected return on assets in the future. A company has a small business risk if the demand for the product is stable, the input and product prices are relatively constant, the price of the product can be adjusted immediately with the increase in costs and partly of cost will encourage decline if the production and its sale decrease. The higher risk the higher uncertainties in the future to produce profit (Tarjo, 2008). If other things remain the same, the lower the business risk of the company it will the higher risk of an optimal debt (Bringham and Houston, 2011).

Business risks not only vary from industry to industry, but can also vary between companies from certain industries, and can also change over time. Brigham and Houston (2011) show several factors that can affect the business risk of a company, including:

a. Variability in demand; the more stable a product demand from a particular company, ceteris paribus, will reduce the company's business risk.
b. Variability in selling prices; companies whose products are sold in markets that are relatively volatile (volatile), will have more business risk when compared to the same company whose output prices are more stable.
c. Variability of input costs; companies that have input costs that are uncertain will have a high business risk.
d. Ability to adjust output prices with changes in input costs; the more capable a company is making adjustments in terms of price and costs, the company has a lower business risk.
e. The ability to develop new products in an effective time and cost. Companies such as drugs and computers are very dependent on the innovation of new products. The sooner a product becomes old or obsolete, the greater the risk of the business.
f. Risks from foreign trade; companies whose revenues come mostly from abroad can make the company's revenue decline risk, this is due to fluctuations in the exchange rate. Another thing that can add business risk is the business environment in which the company operates.
g. The proportion of fixed costs to the overall cost: operating leverage; if most of the costs are fixed, which is not down when demand decreases, then the company has a high business risk.

Brigham and Houston (2011) mention in the concept of economics, shareholders bear certain risks caused by the company's operating activities namely business risk. If the company uses debt, this results in all business risks being transferred to shareholders. The transfer of all risks is caused by creditors who receive fixed income (interest on debt), do not bear the business risks that exist.

Measurement of business risk can be done by using the coefficient of variation of profit or surplus (Atmaja, 2008). Business risk in this research is measured by Basic Earning Power (BEP) Ratio. This ratio shows the ability of assets owned to generate returns or income from company assets before the influence of tax and leverage. This is very useful for comparing companies with different tax situations and different levels of leverage (Bringham and Houston, 2006).

III. RESEARCH HYPOTHESIS

The influence of Leverage toward Profitability

Leverage is the use of assets and sources of funds by companies that have fixed costs (fixed costs) with the intention to increase the potential profits of shareholders (Sartono, 2010). Coricelli et al., (2013) states that firm leverage has a negative influence on the profitability of the company because a high level of leverage will have a high risk which is characterized by a greater debt cost. This large debt causes the company's profitability to be more low because the company's attention is shifted from increasing productivity to the need to generate cash flows to pay off their debt. If firm borrows more money from its creditors then the firm has to pay more amount of cost of debt to the creditor which is called interest rate this leads to less net income for the firm and hence lower profitability (Padron and Santana, 2005). Highly profitability firms have lower levels of leverage than less profitable firms because they first use their earning before looking for external capital (Titman and Wessels, 1988).
H1: Leverage influences on profitability

The Influence of Leverage toward Business Risks

Leverage is the ratio that describes the relationship between corporate debt to capital, this ratio can see how far the company is financed by debt or outside parties with the ability of the company described by capital (Harahap, 2013). According to (Munawir, 2002) has shown that leverage ratio is ratio to measure how much asset financed from loan. Leverage is measured by debt ratio toward total asset, that is ratio which measure the company assets financed by debt (Rizqia, 2013). The higher the level of debt the company have, the higher the level of risk received. Companies with high business risk tend to avoid funding by using debt compared to companies with lower business risks (Ratri, 2017). Business risk is uncertainty regarding projected returns on assets in the future. Business risks can change from time to time. Every company will face risks as a result of the company's operating activities, both business risks and debt risks that must be used by the company (Bringham and Houston, 2011). So the lower the business risk of the company, it will be easy of the company increasing risk of debt to optimal level. In a company, business risk will increase if you use high debt. This will also increase the possibility of bankruptcy. The higher risk the higher uncertainties in the future to produce profit (Tarjo, 2008). The higher debt to equity ratio means the companies have much loaned fund to finance their assets, on the contrary the lower the ratio, most of the asset financed by the itself fund (Bangun, 1989). Companies with high risk should use less debt to avoid the possibility of bankruptcy. This shows that there is a relationship between leverage on business risk.
H2: Leverage influences on business risk

The influence Business Risk toward Profitability

Referring to the research conducted by Epayanti (2013) stated that business risk has a positive and significant influence on profitability. The company's business risks are reflected in the use of fixed operating costs so as to increase the company's profitability accompanied by an increase in company sales, increasing sales means increasing the company's profitability. The same thing was stated in the research conducted by Valentina (2017), the results of this study stated that business risk has a positive and significant effect on profitability. If business risk is high the profitability will increase. A high business risk is due to having to pay high interest costs on increased debt. This does not make profitability decrease because when it wants to achieve a high rate of return, it faces a high business risk. The resulting return will be greater and can cover high interest costs on company debt.
H3: Business Risks influence Profitability
The concept of the influence of each research variable based on the description above can be described in the conceptual framework model as follows:

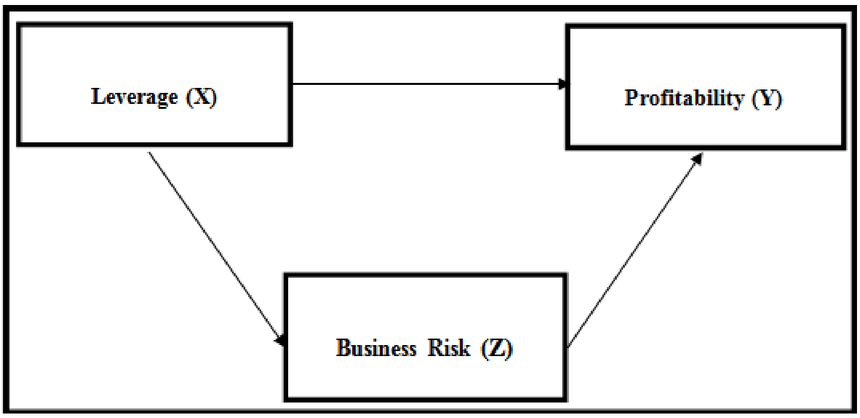

Figure 1. Research Model

IV. METHOD

Data Collection

The data obtained by the researcher are annual financial statements that have been made and recorded in a row during the 2013-2017 period and included in the LQ45 list obtained through the website www.idx.co.id. Samples taken were LQ45 companies listed on the Indonesia Stock Exchange (IDX) in the period 2013-2017 which were in accordance with the criteria that the researcher had determined. Considerations in selecting samples using purposive sampling technique. The criteria for the research sample that the researcher has determined are as follows: (1) Companies listed in the LQ-45 during the period 2013-2017. (2) The companies listed in a row on the LQ45 during the period 2013-2017. The method of analysis in this study was Structural Equation Modeling (SEM) using Partial Least Square (PLS).

Operational Variables and Definitions

Profitability

Profitability is the ratio to assess the company's ability to seek profit (Kasmir, 2012). According to Weston (1999), profitability is the net final results from various policies and decision. Profitability in this study is measured by Return on Assets (ROA). Return on Assets (ROA) which is the ability of the capital invested in all assets to generate profits for all investors (bond holders and shares). Return On Assets (ROA) is a ratio that shows results (return) on the amount of assets used in a company (Kasmir, 2012). Return On Assets can be formulated as follows:

$$\text{Return On Asset (ROA)} = \frac{\text{EAT}}{\text{Total Asset}} \text{ x } 100$$

Leverage

Leverage is a ratio that describes the relationship between corporate debt to capital, this ratio can see how far the company is financed by debt or outside parties with the ability of the company described by capital (Harahap, 2013). According to (Munawir, 2002) has shown that leverage ratio is ratio to measure how much asset financed from loan. The higher debt to equity ratio means the companies have much loaned fund to finance their assets, on the contrary the lower the ratio, most of the asset financed by the itself fund (Bangun, 1989). The leverage of this research is measured by Debt to Equity Ratio (DER). This ratio is used to compare sources of capital derived from debt (long-term debt and short-term debt) with equity. This is usually used to measure financial leverage of a company (Sartono, 2010). Mathematically the calculation of Debt to Equity Ratio (DER) is:

$$\text{Debt To Equity Ratio (DER)} = \frac{\text{Total Debt}}{\text{Total Equity}} \text{ x } 100$$

Business Risk

Business risk is uncertainty about projecting returns on assets in the future (Bringham and Houston, 2001). Business risk in this study is measured by Basic Earning Power (BEP) Ratio. This ratio shows the ability of assets owned to generate returns or income from company assets before the influence of tax and leverage. This is very useful for comparing companies with different tax situations and different levels of leverage (Bringham and Houston, 2006). This ratio is calculated by the formula:

$$\text{Basic Earning Power Ratio} = \frac{\text{EBIT}}{\text{Total Asset}} \text{ x } 100$$

V. RESULT AND DISCUSSION

Uji Goodness of Fit

Table 1

R-Square

Variabel	R-Square
Profitabilitas	0.992269
Resiko Bisnis	0.658246

Source: Processing Results with SmartPLS 2.0

Based on the data in table 5 above, it can be seen that the value of R-Square for the variable profitability is 0.992. The acquisition value explained that the percentage of profitability could be explained by business risk of 99.2%. Then for the R-Square value obtained the Business Risk variable is 0.658. This value explains that business risk can be explained by leverage and profitability by 65.8%.

The assessment of goodness of fit is known from the value of Q-Square. The value of Q-Square has the same meaning as the determination coefficient (R-Square) in the regression analysis where the higher the Q-Square, the model can be said to be better or more fit with the data. The results of the calculation of the Q-Square value are as follows:

Q-Square = 1 – [(1 – $R^2$1) x (1 – $R^2$2)]
= 1 – [(1 – 0,992) x (1 – 0,658)]
= 1 – (0,008 x 0,342)
= 1 – 0,002
= 0,998

Based on the results of the calculations above obtained the value of Q-Square of 0.998. This shows the magnitude of the diversity of research data that can be explained by the research model is 99.8%, while the remaining 0.2% is explained by other factors that are outside of this research model. Thus, from these results, this research model can be stated to have good goodness of fit.

Test Path Coefficient

Path coefficient evaluation is used to show how strong the effect or influence of the independent variable is on the dependent variable, while the determination coefficient (R-Square) is used to measure how many endogenous variables are influenced by other variables.

Table 2

Path Value Coefficients

Variable	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	Standard Error (STERR)	T Statistics (|O/STERR|)	Sig. P	Result
Leverage => Profitability	0.048543	0.059692	0.030617	0.030617	1.585501	0.115	Reject
Leverage =>Business Risk	0.811324	0.833534	0.051572	0.051572	15.73196	0.000	Accepted
Business Risk => Profitability	0.956339	0.944156	0.031176	0.031176	30.675968	0.000	Accepted
T Tabel	1.978238						

Source: Processing Results with SmartPLS 2.0

VI. DISCUSSION

The Influence of Leverage on Profitability

From the results of the hypothesis testing above, it is known that the T-Statistics value of the leverage variable on profitability is 1.585 (T-Statistics <1.978) which means NOT SIGNIFICANT and the value of Sig. P on the variable leverage on profitability is 0.115 (Sig. P> 0.05) which means the hypothesis is rejected, so that it can be stated that leverage has no significant influence on profitability. Therefore, it can be concluded that a high level of leverage will cause profitability to decrease because the profits obtained by the company will only be used to pay and pay off debts. In addition, a high level of leverage will increase the level of corporate risk. If firm borrows more money from its creditors then the firm has to pay more amount of cost of debt to the creditor which is called interest rate this leads to less net income for the firm and hence lower profitability (Padron and Santana, 2005). Highly profitability firms have lower levels of leverage than less profitable firms because they first use their earning before looking for external capital (Titman and Wessels, 1988). This is consistent with the findings by Wald (1999), Sheel (1994), Eunju and SooCheong (2005) who concluded that there was an inverse relationship between financial leverage and profitability of firms.

The Influence of Leverage on Business Risks

From the results of hypothesis testing, it is known that the T-Statistics value of the leverage variable on business risk is 15.731 (T-Statistics> 1.978) which means SIGNIFICANT and Sig. P on the variable leverage on business risk is 0,000 (Sig. P <0.05) which means the hypothesis is accepted, so it can be stated that leverage has a positive and significant influence on bussines risk. Therefore, it can be concluded that the greater level of leverage of a company, the more it will increase the level of business risk. If the company does not manage the debt that is used then the company will experience a high risk of bankruptcy.

This is in accordance with Ratri's (2017) that companies with high business risk tend to avoid funding by using debt compared to companies with lower business risks. In a company, business risk will increase if it uses high debt. Companies with high risk should use less debt to avoid the possibility of bankruptcy.

The Influence of Business Risk on Profitability

From the results of hypothesis testing, it is known that the T-Statistics value of the business risk variable on profitability is 30.675 (T-Statistics >1.978) which means SIGNIFICANT and Sig. P on the variable business risk on profitability is 0,000 (Sig. P < 0.05) which means that the hypothesis is accepted, so it can be stated that business risk has a positive and significant effect on profitability. Therefore, it can be concluded that the greater the level of company business risk, the profits that the company can also increase if it can be managed properly. On the other hand, investors who are risk takers will actually be attracted to companies that have a high level of risk because they hold the principle of "High Risk High Return", where the higher the level of risk, the higher the rate of return that will be risked. The higher the profit because many investors invest. This is consistent with the opinion of Epayanti (2013), stating that the company's business risks are reflected in the use of fixed operating costs so as to increase the company's profitability accompanied by an increase in company sales, increasing sales means increasing the company's profitability. According to Syamsudin (1992) in Putri (2009), found that company in their life should be profitable. In here he state that without profit difficult for the company to get capital from external parties.

This is also in accordance with research conducted by Valentina (2017), stating that if business risk is high, profitability increases. A high business risk is due to having to pay high interest costs on increased debt. This does not make profitability decrease because when it wants to achieve a high rate of return, it faces a high business risk. The resulting return will be greater and can cover high interest costs cause of the company has debt.

VII. CONCLUSIONS

Based on the results of the discussion and analysis in this study, it can be concluded that: (1) leverage has no significant influence on profitability. Large debt can cause the profitability of the company concerned because the company's attention is shifted from increasing productivity to the need to generate cash flow to pay off their debt. (2) leverage has a positive and significant influence on business risk. Companies with high risk should use less debt to avoid the possibility of bankruptcy. (3) business risk has a positive and significant effect on profitability. A high business risk is due to having to pay high interest costs on increased debt. This does not make profitability decrease because when it wants to achieve a high rate of return, it faces a high business risk. The resulting return will be greater and can cover high interest costs on company debt.

Based on the results of the discussion and analysis of the study, the authors provide the following suggestions: (1) For companies should consider wisely in using external funds (debt) as operational assistance in increasing profit (profit) because it must be adjusted to the risks that exist in the future day is not at risk of bankruptcy. (2) Further researchers can improve the limitations in this study such as adding or using other variables that can affect profitability and business risk and increase the number of samples and years of observation to improve more complete and accurate information about the company LQ-45.

REFERENCES

[1]. Abdillah, Willy. 2015. Integrated Research Methods of Information Systems. Yogyakarta: CV. ANDI OFFSETAtmaja, Lukas Faithful. 2008. Theory and Practice of Financial Management. Yogyakarta: ANDI Publisher

[2]. Bangun, Darwin. 1989. Company Management. Jakarta. Ministry of Education and Culture Rector General of Higher Education

[3]. Brigham, Eugen And Houston, Joel. 2011. Fundamentals of Financial Management. Jakarta: Salemba Empat.

[4]. Coricelli, G, .et al. 2013. Tax Evasion and Emotion: An Empirical Test of Re-Interactive Shaming Theory. Journal of Economical Psychology.Epayanti, Ayu. 2013. Effect of Company Size and Business Risk on Profitability and Dividend Policy on Manufacturing companies on the IDX. Journal of Udayana University 3488.

[5]. Eunju Yoon & SooCheong Jang (2005). The effect of financial leverage on profitability and risk of restaurant firms. The Journal of Hospitality Financial Managements, 13, 200-210.

[6]. Fahmi, Irham. 2013. Analysis of Financial Statements. Bandung: Alfabeta.Furaida, Yunita Atsni. 2010. Effect of Company Size, Business Risk and Profitability on the Capital Structure of Manufacturing Companies listed on the Indonesia Stock Exchange. Journal of Semarang State University.Ghozali, Imam. 2014. Structural Equation Modeling - Alternative Method with Partial Least Square. Semarang: UNDIP.

[7]. Harahap, Sofyan Safri. 2013. Critical Analysis of Financial Statements. Jakarta: PT. Raja Grafindo.Kasmir. 2012. Analysis of Financial Statements. PT. Raja Grafindo Persada. Jakarta.

[8]. Lukman Syamsudin. (1992). Corporate Financial Management Concept of Applications in Planning, Supervision and Decision Making", Rajawali Pres, Jakarta.Munawir. 2010. Analysis of Financial Statements. 4th Edition. Liberty. Yogyakarta.

[9]. Padron, Y.G., Apolinario, M.C., & Santana, O. (2005). Determinant factors of leverage: An empirical analysis of Spanish corporations, Journal of Risk Management, 6, 60-68.

[10]. Puspida, Sri. 2013. Influence of Business Risks and Growth of Assets on Capital Structure at PT. Java and Bali Generations. Journal of Management Science and Research Vol.

[11]. Ratri, Annisa Mega. (2017). Influence of Size, Liquidity, Profitability, Business Risks and Sales Growth on Capital Structure in the Property Industry Sector. Duta Wacana Christian University Journal. Yogyakarta.

[12]. Rizqia, Ayu Dwita, et. all. (2013). Effect of Managerial Ownership, Financial Leverage, Profitability, Firm Size, and Investment Opportunity Set on Dividend Policy and Firm Value. Journal of Finance and Accounting. Vol. 4. Issue 11. 120-130

[13]. Salim, H.Abbas. 2007. Insurance and Risk Management. Raja Grafindo Persada. Jakarta.

[14]. Sanusi, Anwar. 2013. Business Research Methodology. Jakarta: Salemba Empat.

[15]. Sartono, Agus R, .2010. Financial Management Theory and Application. 4.Yogyakarta Edition: BPFE.

[16]. Sheel, A. (1994). Determinants of capital structure choice and empirics on leverage behavior: A comparative analysis of hotelandmanufacturing firms. Hospitality Research Journal,

[17]. 17, 3-16

[18]. Sholihin, Mahfud and Ratmono. 2013. Analysis of SEM-PLS with WarpPLS 3.0.Yogyakarta: C.V Andi Offset.Sugiyono. 2009. Business Research Methods. Bandung: Ministry of National Education Language Center

[19]. Tanjung, Kautsar. (2017). Analysis of the Effect of Financial Leverage on Profitability on Life Insurance Companies listed on the IDX. Journal of the University of Lampung. Bandar Lampung.

[20]. Tarjo. 2008. Effect of Institutional Ownership and Leverage Concentration on Earnings Management, Shareholder Value and Cost of Equity Capital. National Symposium on Accounting XI Pontianak

[21]. Titman, S. & Wessels, R. (1988), “The determinants of capital structure choice”, Journal of Finance, Vol 43(1), pp. 1–19.

[22]. Valentina, Henni. 2017. Effect of Capital Structure, Business Risks and Sales Complaints on Financial Performance in Real Estate and Property Companies listed on the IDX. Journal Of Management Vol.4.

[23]. Wald, J. K. (1999). How firm characteristics affect capital structure: an international comparison. Journal of Finance Research, 22, 161-188.

[24]. Weston, J. Fred and Eugene Brigham. 1990. Fundamentals of Financial Management. Jakarta: ErlanggaWirartha, I Made. 2006. Socio-Economic Research Methodology. Yogyakarta: CV. ANDI OFFSET

Punandra Cahya N.S" The Influence of Financial Leverage toward Profitability Through Business Risk As Intervening Variables In LQ45 Companies Listed In Indonesia Stock Exchange (2013-2017)" International Journal of Business and Management Invention (IJBMI), vol. 08, no. 02, 2019, pp 49-55