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# Effect Debt Policy On Profitability, And Dividend (Studies On Indonesia State Enterprises)

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***ABSTRACT***

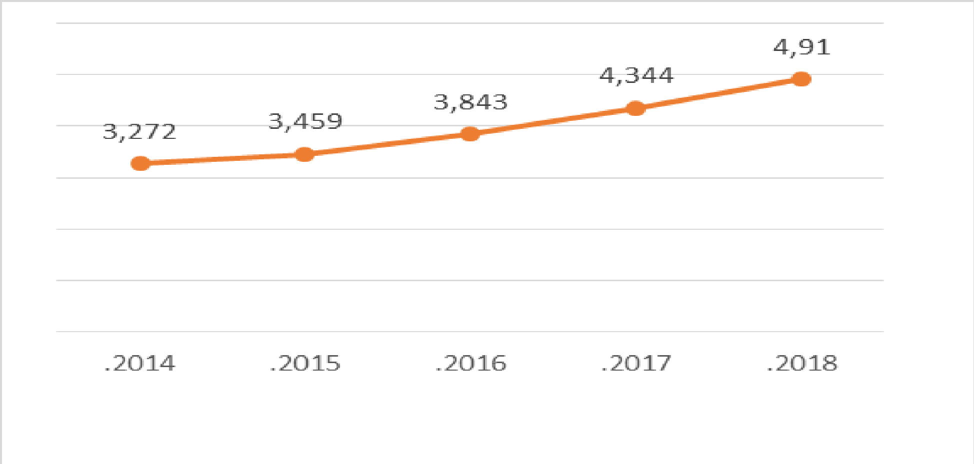
This study aims to examine the phenomenon of debt in state enterprises (BUMN) which is excessive without being followed by an increase in profitability. The sample used is state-owned enterprises (BUMN), the various business sectors for the 2015-2018 period. Using purposive sampling got 137 samples and data processing using the IBM SPSS series 23 program. The result is that debt policy has a negative impact on profitability; it does not prove liquidity to affect profitability. It does not prove liquidity to determine dividends. Debt policy has a negative effect on dividends, and profitability has a positive effect on dividends

**Keywords**: Debt Policy, Profitability, Liquidity, BUMN

## 1. Introduction

State Enterprises (BUMN) are enterprises most of whose shares are owned by the government, according to [1] Law number 19 of 2003 concerning BUMN, the purpose of establishing BUMN is to serve the interests of the public, and as a source to support the APBN. BUMN also has a role in the socio-economic sector, namely as pioneers in the business sector that are not in demand by the private sector. The role of BUMNs as a source of state revenue is an interesting issue to be studied, because many BUMNs whose financial performance does not contribute to the State Budget, actually burden the state. Based on the 2018 BPS report, shows that of the 13 business groups of BUMN during the 2016-2018 period, there were only 5 business groups with positive Return On Equity (ROE), and only 3 business groups with positive Return On Equity (ROA). the amount of debt continues to increase (BPS, 2018) as shown in Figure 1: BUMN debt.
Debt is an alternative source of funds that can be used to meet the investment needs of a company, the use of debt as a source of investment funds is expected to generate returns that are greater than the costs to be paid for the use of the debt. The obligation to pay the cost of the debt is a fixed burden that can increase risk, thus the use of the debt is only justified if the return generated from the debt is greater than the level of costs to be paid. This means that debt policy is the right decision if with this debt, profitability increases. The increase in the amount of debt that is not matched by growth in profitability raises whether this condition shows the use of excessive debt, as explained in the theory of capital structure, that the use of debt has an optimal limit. , the use of debt that exceeds the optimal limit will have a negative impact on performance [2] This profitability condition will also affect dividends, meaning that this debt policy is not under the objectives of the establishment of SOEs. The relationship between debt policy and profitability is explained by [3] that enterprises prefer to use sources of funds from operating results rather than sources of new debt or stock funds because these sources will lead to information asymmetry which will increase the cost of capital which

can ultimately reduce profitability. Testing the relationship between debt and profitability was also carried out by [4] the results found an inverse relationship between capital structure and profitability. Empirical evidence of the relationship between debt and profitability is also explained by [5] using a sample of enterprises listed on the Ghana stock exchange finding a negative relationship between capital structure and profitability, the same thing was found by [6][7] that debt and profitability are inversely related, meaning enterprises that are Many use debt is low in profitability.



Source: BPS 2018 Figur 1: BUMN Debt

Meanwhile, [6] also tested the relationship between liquidity and profitability. The result is that the availability of liquidity from internal sources can reduce the cost of capital, which will further increase profitability, thus liquidity is positively related to profitability. [8] conducted the same study and the results support previous research, which states that liquidity has a positive effect on profitability. Meanwhile, [9] the results of his research found an inverse relationship between liquidity and profitability. According to him, high liquidity shows over-liquidity, so it has a negative impact on profitability. [10] carried out testing the relationship between debt and dividends out, the result is that debt is inversely related to dividends. The existence of an obligation to pay interest can limit the provision of cash to pay dividends. [11] found the same result using a sample of non-financial corporations on the Indonesia Stock Exchange. Meanwhile, the opposite result was found by [12]), in his research using a sample of manufacturing enterprises listed on the South Korean Stock Exchange, and the result is that debt has a positive effect on dividend policy. Meanwhile, the relationship between profitability and dividends is explained [13] using a sample of enterprises listed on the Jordan Stock Exchange finding a positive relationship.

They conducted this research to answer problems related to increasing debt accompanied by low profitability in BUMN enterprises. Low profitability will limit the ability to distribute profits to owners, this is not under the aims and objectives of establishing BUMN. This study places debt and liquidity policies as factors that are predicted to affect profitability. The variables that are predicted to determine dividends are debt policy, liquidity, and profitability.

## 2. Literature Review

The financial literature explains that the dividend decision is one of the strategic decisions that can affect market performance [14]. Although this decision is routinely made by management, it is difficult, because it must consider many aspects. The aspects considered are not only related to the liquidity position but also related to behavioral issues, namely the actions and reactions of parties who have an interest in the financial decisions. The practice of separating ownership and management of the company motivates behavioral considerations, which will have the potential to cause a conflict of interest. Management as a decision-maker is based on the authority delegated by the owner to him, but often management does not act in the interests of the owner of the company but prefers his own interests, therefore monitoring must be carried out, the way is that management is forced to use debt or distribute profits as dividends. 15]. also explained, that management must be disciplined with debt policies because debt can reduce agency conflicts and improve company performance. The rationale is, debt forces management to provide cash to pay interest. Another alternative to control management is to distribute cash as dividends, this is will reduce the use of free cash

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flow for less prospective investments. Dividend policy can reduce agency conflict because it forces management to seek external sources of funds to finance their investments [16]. From this explanation, the meaning is the use of debt and dividend distribution as a substitution policy. From another point of view, profit is the preferred source of internal funds, because the cost is relatively cheap [3]. It is explained in the pecking order theory, that the company has a preference in financing its operations, management prefers to use internal sources, retained earnings rather than debt, this internal source of funds can affect the proportion of cash to be distributed as dividends [17].

Empirical evidence of the relationship between debt policy and dividends shows a negative relationship [18][10] [11]. Meanwhile, [12][13] found a positive relationship between debt and dividends. The dividend decision is also related to profitability, the relationship can be explained that net profit is operating income after all obligations are paid to various parties who contribute to the company, this profit is wholly under the control of the owner of the company, whether wholly or part of the profit will pay as dividend depending on to the owner of the company. As we have seen that dividend payment is a risk compensation borne by investors. Dividends are one of the income received by investors, besides capital gains. The policy to postpone or reduce the income is only justified if it can increase the share price (capital gain) in the future, and this can only be realized if the profit is invested and can generate a positive net present value (NPV). Thus, the dividend policy is a trade-off between the return received today and the capital gain that is expected to be received in the future.

There are different views related to dividend payments, these differing views about how much dividends will be paid, whether as much as possible or vice versa, according to [19][20], and [21], dividends should be divided as much as possible. To shareholders, cash today is more certain than capital gains that are expected to be got in the future. I explained the opposite view in the concept of dividend residual. According to this concept, dividends are the last alternative after they meet all cash needs. The distribution of dividends is the remaining profit after they meet all investment needs. The difference in these concepts illustrates that the relationship between profitability and dividends depends on the view or preference for dividends. Basically, profitability shows the ability to pay dividends, and the company has no obligation to pay dividends if it does not make a profit. Based on this explanation, profitability is the key factor as a determinant of dividend payments, while the amount to be paid as dividends depend on the preferences and priorities of the company's interests. Several previous researchers have tested the relationship between profitability and dividend payments, for example, [13] found a unidirectional relationship between profitability and dividend payments. While [18][22] the results of his research prove the inverse relationship between profitability and dividends. These findings show an inconsistent relationship between profitability and dividends

liquidity is an important component in supporting the company's operations. They defined liquidity as the company's ability to provide liquid assets to meet its operational needs. Adequate liquidity is a requirement for smooth business operations. Limited availability of liquidity can disrupt operational activities which can suppress profitability [23]. Excessive use of liquidity shows that there are idle funds that do not generate income, therefore liquidity needs to be efficient to ensure smooth operations and increased profitability. Often liquidity becomes a burden on the company, this is because the funds tied up in current assets are an opportunity cost, because these funds should be able to be invested and generate income, or vice versa, enterprises with a liquidity deficit must seek short-term loans or sell their liquid assets. Burden. Optimal liquidity management can eliminate these burdens, increasing profitability. Empirical evidence as stated by Gitman, found by [24], in his research, especially on public enterprises in Saudi, found a negative relationship between liquidity and profitability in enterprises with high current ratios, and cash conversion cycles that take a long time. This finding means the quantity of current assets measures liquidity, but the speed of cash conversion also determines the level of company liquidity. [23] also presented empirical evidence of the relationship between liquidity and profitability using the current ratio as a proxy for liquidity and ROA as a proxy for profitability, finding a positive relationship. [25] found the same finding, using a sample of Jordanian trade enterprises listed at the Amman Stock Exchange (ASE) that liquidity, as measured by the Quick ratio, has a positive effect on profitability as measured by Return On Assets. The financial literature explains the relationship between the availability of liquid assets and the payment of dividends. [15] explained that one way to control management is to distribute cash as dividends, this will reduce the use of free cash flow for less prospective investments. The concept explains that the availability of cash needs to be distributed to the owners of the company to avoid investments that are detrimental to investors. The concept explains that dividends are an effort to discipline management because the company has excess liquidity. This means that dividend payments are only possible if the company has sufficient liquidity, the greater the availability of liquid assets, the greater the ability to pay dividends. [26 carried empirical evidence of the relationship between liquidity and dividends out], using a sample of food and beverage enterprises on the Indonesia Stock Exchange, and the results found a positive relationship between liquidity and dividends. [27 carried the same results out], [28] Meanwhile, [ found the results of the study, which found a negative relationship between liquidity and dividends29]

This study will examine the relationship between debt policy and liquidity with profitability and dividends, using a sample of state-owned enterprises based on the relationship pattern as described. This study proposes the following hypothesis:

H1: Debt Policy has an effect on Profitability.
H2 : Liquidity Affects Profitability
H3 : Debt Policy has a negative effect on dividends.
H4 : Liquidity has a positive effect on dividends
H5: Profitability has a positive effect on dividends.

## 3. Research Method

This study aims to examine the relationship between Debt Policy (DE), Liquidity (LIQ), and their effect on Profitability (PROF), and Dividends (DIV). Debt and Liquidity Policy as independent variables, while Profitability and Dividends as dependent variables. The sampling technique used is proportional, based on the established criteria, and got 137 samples of enterprises. the object of this research is to use various state-owned enterprises (BUMN) for the period 2014-2018.

### 3.1. Operational definition.

**Dividend.**

Dividends are part of profits that are distributed to shareholders, as a return on investment and risk coverage. While the measurement of the variable uses the dividend payout ratio, namely the proportion of cash dividends distributed to shareholders compared to the amount of profit [14]. Formulated:

$$DIV = \frac{Cash\ Dividend}{Net\ Income}$$

**Debt Policy.**

Debt is a source of funds got from creditors. To measure the amount of debt in the company using the Debt to Equity Ratio, namely the amount of debt compared to Equity [14]. This study uses debt to total assets as a measure of the use of debt in the company. I planned this debt ratio:

$$DE = \frac{Debt}{Equity}$$

**Profitability**

Profitability is the level of profit got from operating results using the equity in the period [14], and is formulated as follows:

$$PROF = \frac{Net\ Profit}{Equity}$$

**Liquidity.**

Liquidity is the company's ability to meet all short-term obligations, both obligations to external parties and obligations to internal parties, including paying dividends. The current ratio, which is the ratio of current assets to current liabilities, measures this liquidity:

$$LIQ = \frac{Current\ Asset}{Current\ Liability}$$

Analysis.

This study uses multiple regression to measure the effect of the independent variable debt policy (DE), liquidity (LIQ), on the dependent variable profitability (PROF), and dividends (DIV). using the program IBM SPSS series 23. The regression equation is formulated as follows:

$$PROF = \alpha_1 + \beta_1\ DE + \beta_2\ LIQ + e_1 \quad \text{...........................................} (1)$$

$$DIV = \alpha_2 + \beta_3\ DE + \beta_4\ LIQ + \beta_5\ PROF + e_2 \quad \text{...........................................} (2)$$

Where:

$\alpha_1$; $\alpha_2$ = Constant

1; 2; 3; 4; 5 = Regression coefficient.
PROF = Profitability
DIV = Dividend
DE = Debt Policy.
LIQ = Liquidity

## 4. Results and Discussion.

Table 1 descriptive statistics contains the minimum, maximum, mean, and standard deviation values, the variables used in the study: Profitability (PROF), Liquidity (LIQ), Debt Policy (DE), and Dividends (DIV). Profitability means 0.127, with a standard deviation of 0.063; Liquidity mean 0.280 with a standard deviation. This profitability variable has the largest distribution. I can see that the minimum value is 0.280 and the maximum value is 12.995. Debt Policy has a mean value of 1.729 with a standard deviation of 1.139. Variable Dividend mean value 0.368 with standard deviation 0.257

**Table 1**
**Descriptive Statistics**

| Variable | N | Minimum | Maximum | Mean | Std. Deviation |
|---|---|---|---|---|---|
| RROF | 137 | ,009 | ,292 | ,127 | ,063 |
| LIQ | 137 | ,280 | 12,995 | 1,601 | 1,272 |
| DE | 137 | ,077 | 5,113 | 1,729 | 1,139 |
| DIV | 137 | ,023 | ,991 | ,368 | ,257 |

Source: Processed data

**Table II**
**Regression Model 1**

| | Unstandardized Coefficients | | Standardized Coefficients | | |
|---|---|---|---|---|---|
| Model | B | Std. Error | Beta | t | Sig. |
| (Constant) | ,170 | ,019 | | 9,143 | ,000 |
| DER | -,020 | ,006 | -,269 | -3,042 | ,003 |
| CR | -,004 | ,006 | -,062 | -,700 | ,485 |

Dependend: PROF
Source: Data processed

### 4.1. Regression Model 1

Table II, results from testing Model 1 which places profitability (PROF) as the dependent variable, Debt Policy (DE), and Liquidity (LIQ) as independent variables. The results of the regression test model (1) are: The relationship between Debt Policy and Profitability in the Hypothesis (H1), that Debt Policy influences Profitability. Based on the results of statistical testing shows the regression coefficient - 0.020 with a significance value of 0.003 <0.05. According to the results of the test, debt policy has a negative effect on profitability. The results are under the issues described in the background of this study. Using debt continues to increase without being matched by an increase in profitability. This debt position shows the use of debt that exceeds the optimal limit, as described in the Trade-off theory developed by [2]. I stated the relationship between Liquidity and Profitability in the Hypothesis (H2). Liquidity (LIQ) influences profitability (PROF). The results of statistical tests show a regression coefficient (-0.004) with a significance value of 0.485 > 0.485. This result shows that liquidity has no effect on profitability, meaning that liquidity is not a factor that determines profitabilit

### 4.2. Regression Model 2

Table III results from testing Model (2) which places Dividend (DIV) as the dependent variable, while Debt Policy (DE), Liquidity (LIQ), and Profitability (PROF) as independent variables. The results of the regression test model (2) are: The results of statistical testing of the relationship between Debt Policy and Dividends show a regression coefficient of -0.104 with a significance of 0.000 < 0.005. The results of this statistical test interpret that debt policy (DE) has a significant effect on dividends (DIV) with a negative coefficient. A negative value means that debt policy has a negative effect on dividends. Dividend. This finding shows that the debt obligations that must be paid limit the dividend payments of state-owned enterprises. The results of the previous research conducted by [18][10]. The results of hypothesis testing (H4) are related to Liquidity (LIQ) and Dividends (DIV), based on the results of statistical tests showing a regression coefficient of -0.015 with a significance of 0.337 > 0.05, this result means that liquidity has no effect on dividends. These findings are not under the predictions stated in the hypothesis. The relationship between Profitability (PROF) and Dividends (DIV) can be seen from the results of statistical tests, based on the results of statistical tests showing a regression coefficient of 0.643 with a significance of 0.041 < 0.05, this figure means that profitability has a significant effect on dividends, a positive coefficient means that profitability has a positive effect. This result is under the previous prediction that profitability has a positive effect on dividends. The findings support previous research conducted by [13].

**Table III**
**Regression Model (2)**

| | Unstandardized Coefficients | | Standardized Coefficients | t | Sig. |
|---|---|---|---|---|---|
| | B | Std. Error | Beta | | |
| (Constant) | ,490 | ,073 | | 6,735 | ,000 |
| DE | -,104 | ,019 | -,461 | -5,515 | ,000 |
| LIQ | -,015 | ,017 | -,074 | -,886 | ,377 |
| PROF | ,643 | ,312 | ,159 | 2,060 | ,041 |

Dependend Variable : DIV

## 5. Conclusion.

Based on the results of statistical tests, the predicted variables determine profitability, it does not prove liquidity to affect profitability. These results are not under previous predictions. This result is understandable because based on the data got, it shows that debt fulfills the availability of liquid assets to support these operational activities, considering that during the observation period more than half of all BUMN enterprises during the observation period experienced losses. This is also related to the finding of the effect of debt policy on profitability in a negative direction, the negative effect can be concluded that excessive debt burden limits the company in paying obligations the interest expense to be paid is greater than the return received from the investment made. This condition is under the predictions of the trade-off theory, which shows the use of debt that exceeds the optimal limit. The results of the test of factors that are predicted to determine dividends, we can conclude that of the three predicted variables, it proved only two variables affect dividends, namely debt policy and profitability. The effect of debt policy on dividends is negative. This shows that the use of debt for investment activities actually reduces the ability to pay dividends. This happens because the use of debt does not improve the availability of cash to pay dividends. We can conclude the effect of profitability on dividends to have a positive effect, a positive relationship means that dividend payments depend on earnings.

The contribution of the results is to support the trade-off theory.

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