

Corporate Value and the Role of Profitability Mediation: An Empirical Review

Corporate Value and
Profitability
Mediation

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ABSTRACT

This study aims to analyze the role of profit mediation in the relationship between capital structure and dividend policy in increasing the value of the company. This study uses a quantitative method, with secondary data collection techniques from the Indonesian Capital Market Directory (ICMD). The analysis method used Partial Least Square (PLS) with the help of the SmartPLS 3.0 application. The findings of the study show that the capital structure and dividend policy have no effect on the company's value, the capital structure has no effect on profitability, the dividend policy has an effect on profitability, profitability has an effect on the company's value, profitability mediates the effect of dividend policy on the company's value but is unable to mediate the influence of the capital structure on the company's value. Managerial implications for financial practitioners to focus more on managing and developing capital structures and dividend policies to strengthen investor involvement in achieving profitability thereby driving company value. These results also underscore the importance of strategic financial planning that aligns profitability goals with shareholder expectations and market condition.

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Keywords: Capital Structure, Company Value, Dividend Policy, Profitability, Profit Mediation.

ABSTRAK

Penelitian ini bertujuan untuk menganalisis peran mediasi keuntungan pada hubungan struktur modal dan kebijakan deviden dalam meningkatkan nilai perusahaan. Penelitian ini menggunakan metode kuantitatif, dengan teknik pengumpulan data sekunder dari Indonesian Capital Market Directory (ICMD). Metode analisis menggunakan Partial Least Square (PLS) dengan bantuan aplikasi SmartPLS 3.0. Temuan penelitian menunjukkan bahwa Struktur modal dan kebijakan deviden tidak berpengaruh terhadap nilai perusahaan, Struktur modal tidak berpengaruh terhadap profitabilitas, Kebijakan deviden berpengaruh terhadap profitabilitas, Profitabilitas berpengaruh terhadap nilai perusahaan, profitabilitas memediasi pengaruh kebijakan deviden terhadap nilai perusahaan namun tidak mampu memediasi pengaruh struktur modal terhadap nilai perusahaan. Implikasi manajerial bagi praktisi keuangan untuk lebih fokus dalam mengelola dan mengembangkan struktur modal dan kebijakan deviden untuk memperkuat keterlibatan investor dalam meraih profitabilitas sehingga mendorong nilai perusahaan. Hasil ini juga menggarisbawahi pentingnya perencanaan keuangan strategis yang menyelaraskan tujuan profitabilitas dengan harapan pemegang saham dan kondisi pasar.

Kata kunci: Struktur Modal, Nilai Perusahaan, Kebijakan Dividen, Profitabilitas, Mediasi Laba.

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INTRODUCTION

In the face of increasingly fierce market competition, companies must continuously grow to ensure long-term sustainability. To achieve this, they must set clear and strategic goals that serve as operational guidelines. These goals include maximizing shareholder wealth, generating optimal profits, ensuring customer satisfaction, increasing firm value, and sustaining business longevity (Irfani, 2020; Muchtar, 2021). The firm's value, which reflects the price that potential shareholders are willing to pay in the capital market, is a critical indicator of success (Muliana & Ikhsani, 2019; Toni & Silvia, 2021). For investors, firm value commonly reflected in share prices is a crucial metric in assessing performance and prospects (Supriadi et al., 2024). An increase in share price signals public trust and confidence in the company's future performance, which simultaneously supports shareholder prosperity. Despite the importance of firm value, determining what factors significantly affect it remains an ongoing challenge. Among the key financial variables influencing firm value are capital structure, dividend policy, and profitability. Capital structure, especially the use of debt, is central to the trade-off theory which argues that firms can enhance value by leveraging tax advantages and reducing agency costs so long as financial risks are contained (Irfani, 2020; Olii et al., 2021). Empirical studies by Amelia and Anhar (2019), Nurmatias (2019), and Suzulia et al. (2020), support this view, finding that optimal capital structure positively influences firm value. Conversely, Wicaksono and Mispiyanti (2020) reported that capital structure does not significantly impact firm value, indicating inconsistency in empirical findings.

Dividend policy is another influential factor. Based on the bird-in-the-hand theory, investors prefer receiving dividends over uncertain capital gains, which makes dividend distributions an important signal of financial health (Darmawan, 2018; Dolongseda et al., 2020). The signaling theory further supports that rising dividend are positively associated with increasing share prices, reflecting market confidence (Wijaya et al., 2024). A consistent dividend policy not only signals strong future prospects but also builds investor trust and contributes to profitability growth (Tantono & Candradewi, 2019). This link between dividend policy and firm value is reinforced by studies from Aniqoh and Budiantoro (2019), Sari et al. (2020), and Yunarsi (2020). However, different findings from Suardana et al. (2020) indicate that dividend policy may not significantly affect firm value, further highlighting inconsistent empirical results.

Profitability plays a pivotal mediating role in linking capital structure and dividend policy to firm value. It represents the company's ability to generate returns from its operations and is the outcome of strategic decision-making (Sumiati & Indrawati, 2019; Yanti & Setiawati, 2022; Indradewa & Sri Damayanti, 2025). A high level of profitability sends positive signals to the market, attracting investor interest, increasing stock demand and price, and ultimately boosting firm value (Komala et al., 2021). According to Suzulia et al. (2020), profitability mediates the effect of capital structure on firm value, while Paminto et al. (2016) found that profitability also mediates the effect of dividend policy on firm value. These findings affirm that profitability does not only influence firm value directly, but also serves as a bridge that strengthens the impact of capital structure and dividend policies.

Despite numerous studies, empirical findings remain inconclusive. Some research finds no direct impact of capital structure or dividend policy on firm value, while others identify profitability as a partial or full mediator in this relationship. These inconsistencies highlight a theoretical and empirical gap, particularly regarding how profitability functions as an intermediary variable. Therefore, this study aims to examine the mediating role of profitability in the effect of capital structure and dividend policy on firm value, using Indonesian public companies as the research context. Although various studies have explored the individual and mediating effects of these variables, inconsistencies remain in their findings. Some research supports a positive and significant relationship, while others report negligible or no impact. This discrepancy indicates a research gap that must be addressed, especially in understanding how profitability

functions as a mediator in the relationship between capital structure, dividend policy, and firm value.

LITERATURE REVIEW & HYPOTHESIS DEVELOPMENT

Capital Structure, Dividend Policy, Profitability, and Company Value

Ramadanti et al. (2024) stated that company value reflects investor perception of firm performance, and it is closely related to capital structure, dividend policy, and profitability. According to trade-off theory, firms aim for an optimal capital structure to balance tax benefits from debt with financial distress risks (Riduwan, 2018). Companies with proper debt levels can increase firm value by utilizing cheaper financing sources. However, the pecking order theory suggests internal financing is preferable to avoid high external risk (Irfani, 2020). Amelia and Anhar (2019), Nurmatias (2019), and Suzulia et al. (2020) empirically support the role of capital structure in enhancing firm value, though Wicaksono and Mispiananti (2020) argue otherwise. Dividend policy also plays a key signaling role. Darmawan (2018) notes that dividend payments can reflect financial strength and align with the bird-in-the-hand theory. Wijaya et al. (2024) emphasize that dividend increases correlate with higher market value. Aniqoh and Budiantoro (2019), Similarly, Sari et al. (2020), and Yunarsi (2020) found that consistent dividend policies elevate investor trust and firm valuation. Conversely, Suardana et al. (2020) challenge this generalization based on firm-specific factors. Profitability, defined as the company's ability to generate earnings, directly affects firm value (Komala et al., 2021; Laksono & Rahayu, 2021). High profitability not only draws investor attention but also supports long-term valuation growth. Studies by Paminto et al. (2016) affirm its mediating role in financial decision-making outcomes.

H1: Capital structure has a significant effect on company value.

H2: Dividend policy has a significant effect on company value.

H3: Profitability has a significant effect on company value.

Capital Structure, Dividend Policy, and Profitability

Capital structure and dividend policy influence not just valuation, but also profitability. According to Irfani (2020), using debt wisely helps reduce tax burdens while increasing available resources for productive activities, which improves profitability. Ariawan and Solikahan (2022) assert that an optimal capital structure contributes to efficient operations and better financial performance. Supriadi et al. (2024) also support this notion, aligning with the trade-off theory, suggesting a balanced approach to debt use improves returns without risking stability. Nurmatias (2019) along with Santoso and Budiarti (2020) and Suzulia et al. (2020) provide empirical evidence that capital structure positively impacts profitability. Ramadanti et al. (2024) also stated that financial flexibility allows firms to take advantage of investment opportunities, increasing operational returns and stakeholder confidence.

Dividend policy is also found to influence profitability. From the signaling theory perspective, dividends signal stability and performance (Tantono & Candradewi, 2019). Purnama (2020) noted that regular dividend payments improve investor perception and encourage investment, which in turn strengthens profitability. Furthermore, Sumiati and Indrawati (2019) argue that dividends, seen as a form of corporate responsibility, reflect financial integrity and boost brand image. Thus, both capital structure and dividend policy do not act independently but work synergistically in enhancing profitability, which plays a strategic role in sustainable performance.

H4: Capital structure has a significant effect on profitability.

H5: Dividend policy has a significant effect on profitability.

Capital Structure, Dividend Policy on Company Value Through Profitability

The relationship between financial decisions and company value becomes clearer when examined through the lens of profitability. Ramadanti et al. (2024) explained that profitability not only reflects operational efficiency but also mediates financial policy effects on market valuation. According to signaling theory, well-managed debt levels indicate financial health and are positively interpreted by the market (Wijaya et al., 2024). When companies use debt optimally, they increase profitability by gaining tax benefits and leveraging cheaper capital sources. Suzulia et al. (2020) found that profitability mediates the effect of capital structure on firm value, as it demonstrates the efficient use of debt for productive gains. This is aligned with Irfani (2020) and Muchtar (2021), who emphasize that improved profitability due to proper financing decisions boosts investor confidence and enhances valuation.

Likewise, dividend policy influences firm value through profitability. Paminto et al. (2016) highlight that dividend encourage positive investor sentiment, which increases demand and stock price. Simanjuntak et al. (2021) also note that consistent dividend payments signal long-term growth potential. As profitability improves, it reinforces these signals, amplifying the positive impact on firm value. Capital structure and dividend policy must be strategically managed to enhance profitability, which in turn elevates firm value. This indirect path illustrates the critical mediating role of profitability in aligning financial management with market expectations.

H6: Capital structure has a significant effect on company value through profitability.

H7: Dividend policy has a significant effect on company value through profitability.

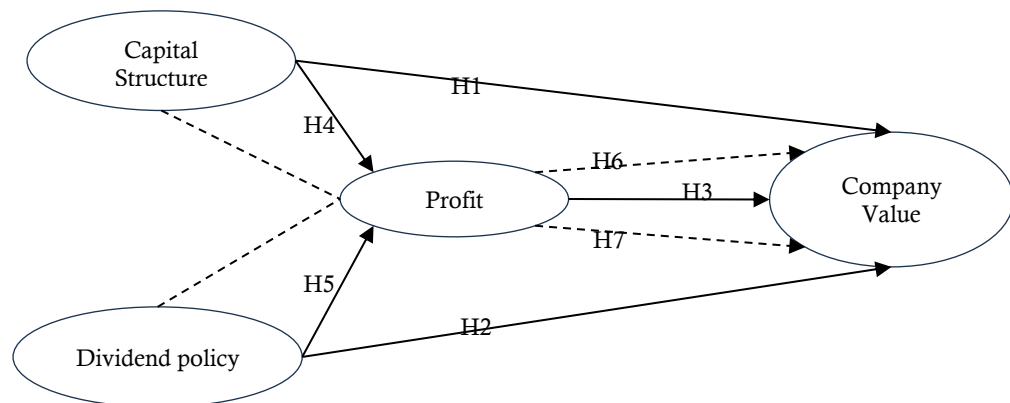


Figure 1. Research Framework

Figure 1 showed a conceptual model that describes the relationship between capital structure (CapStruct), dividend policy (DiviPolic), and profitability (Profit) to company value (CompVal). The capital structure variable is measured by the Debt Equity Ratio (DER), dividend policy is measured by the Dividend Payout Ratio (DPR), profitability is measured by Return on Equity (ROE), and company value is measured using Price to Book Value (PBV). In this model, CapStruct and DiviPolic have a direct effect on Profit, which then mediates the influence of both on CompVal. In addition, CapStruct and DiviPolic also have a direct effect on CompVal, illustrating the existence of a direct or indirect relationship through Profit as a mediating variable.

RESEARCH METHOD

This study employs a quantitative research design to explore the effects of capital structure and dividend policy on firm value, with profitability as a mediating variable. The research focuses on companies listed in the Kompas100 index on the Indonesia Stock Exchange (IDX) from 2016 to 2020. The Kompas100 index was selected due to its representation of Indonesia's most actively traded and fundamentally strong companies, making it a suitable proxy for assessing investor behavior and financial policy implications

in the capital market. These companies are generally more consistent in publishing audited financial statements and are actively monitored by investors and analysts, thus ensuring data reliability. The purposive sampling technique was applied based on three key criteria, first companies consistently listed in the Kompas100 index during the 2016–2020 period, second availability of complete and audited financial data including variables such as DER, DPR, ROE, and PBV, and third companies that did not experience mergers, acquisitions, or significant structural changes during the observation period to avoid data distortion.

The study uses secondary data sourced from the Indonesian Capital Market Directory (ICMD), as well as annual financial reports published on the IDX's official website. The operational definitions of the research variables are as follows: firm value is measured using Price to Book Value (PBV), which reflects market perception and valuation of a company's equity; capital structure is represented by the Debt to Equity Ratio (DER), indicating the proportion of debt used relative to equity; dividend policy is measured by the Dividend Payout Ratio (DPR), which shows the portion of earnings paid out to shareholders; and profitability is assessed using Return on Equity (ROE), capturing the company's ability to generate profits from shareholder equity. These indicators were selected because they are widely used in prior research and provide a clear reflection of financial policy and performance.

To analyze the data, this study uses Partial Least Squares Structural Equation Modeling (PLS-SEM) via SmartPLS 3.0. This method is appropriate due to its ability to handle complex variable relationships without requiring normality or large samples. The analysis includes two stages: evaluating the measurement model (outer model) and the structural model (inner model). Indicator reliability is tested using outer loadings (≥ 0.70), while construct reliability is assessed through Composite Reliability and Cronbach's Alpha (both ≥ 0.70). Convergent validity is measured using AVE (≥ 0.50), and discriminant validity is evaluated through the Fornell-Larcker criterion and cross-loadings. The inner model analysis evaluates path coefficients to assess the strength and direction of variable relationships. R^2 measures how much variance in the dependent variable is explained by the model, while Q^2 tests its predictive relevance. Hypotheses are tested using bootstrapping with 5,000 resamples, with significance determined at $p < 0.05$. These steps aim to provide theoretical and practical insights into how firms can optimize capital structure and dividend policy to improve profitability and enhance firm value.

RESULTS

The value of outer loading from the capital structure (X1), dividend policy (X2), profitability (Z) and company value (Y) is at $1 > 0.7$. So that the indicator is declared valid and accepted. The AVE (Ave Variance Extracted) value meets the above conditions of 0.5. The AVE value of Capital Structure, Dividend Policy, Profitability, and Company Value is at $1 > 0.5$. Thus, the predictor is declared valid and accepted. Cronbach's Alpha of each variable has a value of $1 > 0.7$ and the Composite Reliability of each variable has a value of $1 > 0.7$.

Table 1. Fornell-Larcker Criterion Values

Variable	Dividend Policy	Company Value	Profitability	Capital Structure
Dividend Policy (X2)	1.000			
Company Value (Y)	0.363	1.000		
Profitability (Z)	0.74	0.938	1.000	
Capital Structure (X1)	-0.024	0.045	0.123	1.000

Table 1 shows the correlation matrix between variables in the study, namely dividend policy, company value, profitability, and capital structure. The correlation results show that dividend policy has a fairly strong positive correlation with profitability of 0.740 and a moderate correlation with company value of 0.363. Meanwhile, profitability has a very strong correlation with company value of 0.938, indicating that increasing profitability

has the potential to greatly increase company value. On the other hand, capital structure shows a very weak correlation with all other variables, namely only 0.123 with profitability, 0.045 with company value, and -0.024 with dividend policy, indicating a relationship that is almost insignificant. Overall, this table illustrates that profitability is a key variable that has a close relationship with company value and dividend policy.

Then all constructs are accepted and meet the reliability criteria. The Fornell-Larcker value of each latent variable is higher than the value of the other variables, each variable has a value of 1. So that the research instrument has good discriminant validity (Hardisman., 2021).

Table 2. R-Square Values

Dependent Variable	R Square	R Square Adjusted
Company Value (Y)	0.884	0.882
Profitability (Z)	0.157	0.146

Table 2 presents the R Square and Adjusted R Square values for the dependent variables in the research model, namely company value and profitability. The R Square value of 0.884 for the company value variable indicates that 88.4% of the variation in company value can be explained by the independent variables in the model, namely capital structure, dividend policy, and profitability. The Adjusted R Square value of 0.882 confirms that the model remains robust even though it has been adjusted for the number of predictors. Meanwhile, for the profitability variable, the R Square of 0.157 indicates that only 15.7% of the variation in profitability can be explained by capital structure and dividend policy, with an Adjusted R Square of 0.146. This indicates that the model is stronger in explaining company value compared to profitability as an intermediary variable.

The R-Square value at the company value is 0.882 or 88.2%. This means that the model is able to explain 88.4% of the relationship between the influence of the variables studied on the company's value variables. Meanwhile, 11.6% came from variables that were not studied. This model is categorized as a powerful model. The R-Square value on profitability is 0.157 or 15.7%. This means that the model is able to explain 15.7% of the relationship between the influence of the variables studied on profitability. Meanwhile, 84.3% came from variables that were not scrutinized. Models are categorized as weak models.

Table 3. Construct Cross validated Redundancy

Variable	SSO	SSE	Q ² (=1-SSE/SSO)
Dividend Policy (X2)	145.000	145.000	
Company Value (Y)	145.000	18.376	0.873
Profitability (Z)	145.000	123.645	0.147
Capital Structure (X1)	145.000	145.000	

Table 3 shows the results of the Q² value or predictive relevance based on the SSO (sum of squares of observations) and SSE (sum of squares of errors) values for each variable. The company value variable has a Q² of 0.873, indicating that the model has very good predictive ability for the variable. This value indicates that 87.3% of the variability of the company's value can be predicted correctly by the model. Meanwhile, the profitability variable has a Q² value of 0.147, indicating that the model's predictability of profitability is in the weak to moderate category. For the dividend policy and capital structure variables, the SSE value is the same as the SSO, so the Q² value is not available (zero or irrelevant), meaning that these variables are predictors, not endogenous variables in the model.

The Q-Square value for company value is 0.873 and the Q-Square value for profitability is 0.147. The two Q-Square values of each bound variable are > 0.02. With this, it can be stated that the model has a good predictive value of relevance, and the model developed in this study can be accepted and observed (Hardisman., 2021). This

test is to validate the combined performance of the outer model and the inner model whose value is between 0-1. GoF value = 0.72. The resulting GoF value is above the value of 0.36 ($GoF \geq 0.36$) which means that GoF has a large value. With this, it can be stated that the research model has good observation values and the combined performance of the outer model and the inner model are valid (Setiawan, 2017). Test the hypothesis whether the previously developed coefficient influence model is statistically meaningful or not. Hypothesis testing by looking at the significance value of direct or indirect influences, the hypothesis is accepted if the significance is a $t >$ value of 1.96 or a $P <$ value of 0.05.

Table 4. Hypothesis Test

Path Coefficients	Original Sample (O)	Sample Mean (M)	STDEV	t Statistics	p Values
X1 -> Y (H1)	-0.071	-0.070	0.048	1.480	0.140
X2 -> Y (H2)	0.009	0.010	0.038	0.230	0.818
Z -> Y (H3)	0.943	0.944	0.036	26.370	0.000
X1 -> Z (H4)	0.132	0.129	0.077	1.716	0.087
X2 -> Z (H5)	0.378	0.378	0.078	4.820	0.000
X1 -> Z -> Y (H6)	0.124	0.121	0.071	1.740	0.083
X2 -> Z -> Y (H7)	0.356	0.359	0.082	4.340	0.000

Based on Table 4, the direct influence test showed that the H3 hypothesis, H5, had a significant influence on the accepted because the t-statistical value was > 1.96 and the p-value < 0.005 . This means that there is a significant influence between profitability on company value, with a positive direction of 0.943 or 94.3% and there is a significant influence between dividend policy on profitability, with a positive direction of 0.378 or 37.8%. while the hypothesis H1, H2, H4 has no influence because the t-statistical value is < 1.96 and the p-value is > 0.05). This means that there is no significant influence between the capital structure and dividend policy on the company's value as well as the capital structure on profitability. The indirect influence test on the H6 hypothesis found that profitability is not able to mediate the influence of capital structure on the company's value because the Statistics t-value < 1.96 and the P Values > 0.05). While the H7 hypothesis, profitability is able to mediate the influence of dividend policy on the company's value, with a positive influence direction of 0.356 or 35.6%, then profitability is said to be a perfect mediation variable (Sugianingrat et al., 2021).

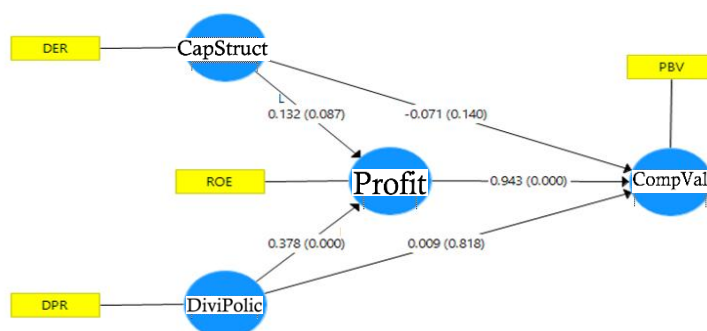


Figure 2. Research Results

The Figure 2 shows the structural model of the PLS analysis results that describe the relationship between capital structure (CapStruct), dividend policy (DiviPolic), profitability (Profit), and firm value (CompVal). Capital structure has an insignificant direct effect on firm value (-0.071; $p = 0.140$), but has an indirect effect through profitability (0.132; $p = 0.087$). Dividend policy also has no direct effect on firm value

(0.009; $p = 0.818$), but has a significant effect on profitability (0.378; $p = 0.000$) which then significantly increases firm value (0.943; $p = 0.000$). These results confirm that profitability is a key mediator in the relationship between capital structure and dividend policy on firm value.

DISCUSSION

The research findings conducted by Irfani (2020), Supriadi et al. (2024) provide important insights into how capital structure, dividend policy, and profitability interact in shaping firm value. The insignificant relationship between capital structure and firm value indicates that reliance on high leverage as evidenced by DER exceeding the optimal threshold has not been effective in increasing market valuation. This indicates a misalignment with the ideal point proposed by the trade-off theory, which recommends a balance between tax benefits and financial risks. The results of the study confirm Wicaksono and Mispiyanti (2020) and Yunarsi (2020), but challenge the conclusions of Nurmatias (2019), Santoso and Budiarti (2020), and Yurinisia et al. (2024), who observed that a well-managed capital structure can have a positive or negative impact on firm value depending on its composition and efficiency. Similarly, dividend policy was found to have no significant direct effect on firm value by Hidayati and Hwihanus (2024). This supports the theory of dividend irrelevance, which states that firm value is more influenced by operational performance and investment opportunities than by payout decisions.

According to Alamsyah (2017), the capital market in Indonesia which is characterized by high liquidity and speculative behavior investors may prioritize capital gains over dividends, thereby limiting the effect of dividend signals. This finding echoes the findings of Paminto et al. (2016) and Suardana et al. (2020), but differs from the research of Aniqoh and Budiantoro (2019), Sari et al. (2020), and Selvy and Esra (2022), which found a positive dividend-value relationship. This suggests that dividend signals may be more effective in certain industries or during periods of economic uncertainty when investor confidence is more sensitive to distribution patterns. However, profitability has a significant positive effect on firm value, which strengthens the signaling theory as stated by Irfani (2020), Halim (2021) and Ariawan (2023) because as a measure of operational efficiency and financial health of a company, high profitability attracts investors and contributes to higher stock prices. This finding is in line with previous studies by Suzulia et al. (2020), Laksono and Rahayu (2021), and Komala et al. (2021), but contradicts the insignificant effects reported by Amelia and Anhar (2019) and Santoso and Budiarti (2020), which highlight contextual gaps that may be related to sectoral differences or firm-specific risk profiles.

Theoretically, this study confirms the important role of profitability as a transmission mechanism in financial decision making. Interestingly, while dividend policy significantly increases profitability supporting the argument that stable dividends strengthen investor confidence and stimulate future profits, according to the views of Komala et al. (2021) and Wijaya et al. (2024) capital structure does not show such an effect. This implies that increasing the debt level can increase liabilities without improving financial results, as also shown by Sugeng (2017), Purnama (2020) and Ariawan and Solikahan (2022). These results emphasize the importance of not only managing the debt ratio but also ensuring that debt is used effectively to generate profits.

The mediation effect of profitability shows different dynamics. This study confirms that profitability significantly mediates the relationship between dividend policy and firm value, consistent with Paminto et al. (2016) and Tantonno and Candradewi (2019), which reinforce the importance of profitability as a channel for value creation. In contrast, profitability fails to mediate the relationship between capital structure and firm value, likely due to inefficiencies in utilizing debt financing, as argued by Sofia and Farida (2017), Nurmatias (2019), and Adam et al. (2025).

CONCLUSION

Based on the findings of this study, it can be concluded that capital structure and dividend policy do not have a direct significant effect on company value, nor does capital structure significantly influence profitability. However, dividend policy is found to significantly and positively affect profitability, and profitability, in turn, has a strong and significant effect on company value. Furthermore, profitability serves as a perfect mediating variable in the relationship between dividend policy and company value, but not in the relationship between capital structure and company value. The practical implication of these findings suggests that companies should prioritize strategies aimed at increasing profitability, as it plays a crucial role in enhancing firm value. Improving dividend policy can attract investor confidence and stimulate profitability, which ultimately boosts company value. Therefore, financial managers are advised to manage dividend distribution strategies effectively while also striving for a more optimal capital structure that supports long-term performance.

Theoretically, this study supports signaling theory, which posits that profitability and dividend distribution serve as positive signals to investors regarding a company's prospects. The findings also align with trade-off theory in emphasizing the need for balanced debt levels in the capital structure to mitigate financial risk. This study is limited by the scope of its sample, which only includes companies listed in the Kompas100 index for the 2016–2020 period, and does not account for macroeconomic factors or industry-specific influences that may affect capital structure, profitability, and firm value. Future research is recommended to expand the sample across different sectors or time periods and to include other moderating or mediating variables, such as firm size or market conditions, to provide a more comprehensive understanding of these relationships.

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