Investment Opportunity Set As The Driver Of Company Value With Capital Structure, Dividend, And Profit Management

Sri Mangesti Rahayu

Abstract: The purpose of the research is to examine the effect of investment opportunity sets on capital structure, dividend, profit management, and its impact on company value. The type of this research is explanatory research and an archival research. The population in this study is a manufacturing company listed on Indonesia Stock Exchange within the period of 2005-2015. The sampling method used in this study is purposive sampling. The research samples is 450 research data. The findings of this research is (1) investment opportunity set has a significant effect on capital structure, not significantly influenced the dividend, a significant impact on earning management, a significant effect on the value of the company; (2) capital structure has a significant effect on profit management, not-significant effect on the value of the company; (3) dividend has a significant effect on the value of the company; (4) profit management has a significant effect on the value of the company. The main originalities proposed by the researchers is the researchers want to test whether the variable of capital structure influence the profit management, to test whether the profit management is opportunistic or informative. This study will use either the accrual basis profit management or real earning management activities.

Index Terms: Capital Structure, Company Value, Divident, Investment Opportunity, Profit Management

1 Introduction

One of the company's goals is to maximize the company value for the benefit of shareholders. The value of a company is the price of an enterprise viewed by an outsider. The maximization of a company value is synonymized to the maximization of company's profits. The company will strive to earn profits as much as possible. The bigger the company's profit, the better the reputation. The company's reputation can be reflected in the stock exchange (stock price of the company) and the access to get credit from the creditors. There are several debates about how much a company's value should be maximized, who benefits the maximization of this company value, and how to maximize it. To date, agency theory becomes the main basis in business to maximize the value of the company. It is stated that there is a separation between the principal as the owner of the company and the agent as the directors of the company so that the agent needs to be convinced to act on behalf of the principal (Jensen & Meckling [20]). Based on the agency theory, there are two main opinions in concern to the benefit of maximizing company value; first, for shareholders and, second, for managers (Grossman & Stiglitz [15]).

First, the benefit of company value maximization for shareholders. Shareholders will require the company's management to work hard and do everything to maximize the value of its stock. Increasing shareholder value can be achieved by increasing profits through investments only on projects that generate a substantial rate of return for the company. Shareholders also demand companies to be as efficient as possible by reducing costs such as production costs, raw materials, and labor for greater profits. The subsequent shareholders demand to share this large profit in the form of dividends. Second, it is assumed that maximizing company value should be part of the manager. Managers feel that company's profits are the result of their hard work so that it is right for them to receive the largest share of the profits. If the shareholder of the company believes otherwise, the manager will act opportunistically to maximize its utility. Opportunistic acts are often associated with bonus contracts. Initially, the bonus contract was created by the shareholder as a principal to motivate the rational agent to act on behalf of the principal when the agent's interest is in contrast with the principal's wish (Scott [33]). Performance-based bonuses are the largest share of total executive earnings. Performance is measured by accounting figures that can be managed opportunistically by the executive to maximize their bonus earnings. There are many ways to achieve company goals in order to increase company value. Managers do not always have to create company value because there is an inherent risk that already exists within the company. These inherent risks include a set of investment opportunity. The effect of this set of investment opportunities on company value is based on agency theory and signaling theory. The agency theory states that the goal of a manager is to maximize shareholder value that can be met by realizing the set of investment opportunities into real growth (Ehie & Olibe [13]). While on the other hand, the signaling theory argued that if there is a positive signal, investors will be interested to buy the company's stock so that the stock value of the company will be increased. Conversely, if the information is negative, investors tend to release the shares of the company (Bhushan [5]). A set of high investment opportunities will be a positive signal for the market that can ultimately increase the value of the company. Besides being an inherent factor, the value of the company can also be enhanced through the company's management policy. In increasing the value of the company, company's management policy can be in the form of a financial policy that affects the company's operations and accounting policies which only influence the company's financial statements. Financial policy is obtained through capital structure and dividend. Meanwhile, accounting policy is constructed by profit management. The influence of capital structure, dividend, and profit management on company value has been proven empirically by Arif [3], Iturriaga and Crisostomo [19], and Cheng et al. [9] which examined the effect of capital structure on company value. Stevens and Jose [35], Pinkowitz [31], Iturriaga and Crisostomo [19] also revealed the effect of dividends on

- *Sri Mangesti Rahayu, Associate Professor in the Faculty of Administrative Sciences,University of Brawijaya, Indonesia, PH-(0341) 551611. E-mail: mangesti_ub@gmail.com*

company value. On the other hand, Tucker and Zarowin [36], Jiraporn et al. [21], Kusumawardhani and Siregar [23] studied the effect of profit management on company value. One important issue in this study is the way in which a management creates a company value that iscapable to accurately reflect the company's true potential and capability. The issue is closely related to the company's financial policies and accounting policies. Financial policies are operational, harder to do, but the impact can be long-lasting while accounting policies are easy to do because it is only related to the financial statements on paper. Good financial policies without proper accounting policies will lead to companies that have low value due to the inability to show it. Otherwise, great accounting policies without proper financial policies will undermine the value of the company. The examples of good financial policy without proper accounting policy are the release of shares of the government of the Republic of Indonesia which are strategic and control the livelihood of the people who are rated very low by investors such as the shares of PT Telkom, PT Indosat (Hadi [16]), and PT Garuda Indonesia (Noor, [30]). These state-owned companies have strategic business areas which control the livelihood of many people in Indonesia as an inherent factor. These companies turn into companies that able to contribute substantial dividends to the Anggaran Pendapatan dan Belanja Negara (State Budget or APBN) annually through appropriate financial policies. The accounting policies of these companies have only been used as a compliment since the only party which has an interest in the financial report is the government. These strategic companies ultimately become a resource that needs to be released to save the deficit of the State Budget when the government is experiencing such financial difficulties. As its release is often in a sudden state, the unpreparedness of the management to make accounting policies which can present the company's excellence and the state condition which is deemed risky due to the deficits, make the value of the company far below the true value in the eyes of investors. There are two examples of great accounting policies without proper financial policies. First is the case of Enron bankruptcy. Enron was a giant energy manufacturing company with natural gas as one of its businesses. This bankruptcy is triggered by the company's accounting policy in the form of opportunistic profit management which ultimately becomes an accounting fraud. Enron raised its profits too high but this high profit was earned by raising its discretionary accruals especially on transactions with related parties, such as its subsidiaries, due to the weak supervision from the board of commissioners. A public accountant, Arthur Andersen, who is the management consultant and had been auditing Enron for many years affirmed that the profit management changed into an accounting fraud. The Enron scandal, which only had big profits on paper but poor operational conditions, was revealed when the company finally went bankrupt in 2001. There are similar cases in other companies after Enron Scandal in 2001-2002 such as Worldcom, Tyco, and Adelphia. The second example is the bankruptcy of an investment bank, Lehman Brothers. Lehman Brothers is a company that emphasizes the growth of shareholder value but have no concern for the stakeholders. Originally, only the client who is considered fit and able to repay the debt would get the credit. However, when all the creditors are assumed worthy to get a credit, the manager still required to increase the shareholder value so that it creates a sub-prime mortgage in the housing loans sector. Debtors who have a little ability to pay their credit back are still given a credit. The subsequent receivables will be pledged to other banks or investment banks which these banks will pledge it to other banks on an ongoing basis. In the end, when the first debtor failed to pay, Lehman Brothers went bankrupt. This bankruptcy continues to spread to banks and other investment banks which pledged the receivables. Due to the big number of bankrupt companies, many employees lose their jobs. These bankrupt companies are mostly multinational companies so that this crisis, started from companies in the United States, spread and became a global crisis in 2008. During the disbursement of debt, Lehman Brothers' financial statements have a good report because of the continued funding growth. A false financial policy to finance an improper party will disturb the operations of the company. Although it does not appear in the financial statements, this could lead to the destruction of the company. This study will also assess how a company management in Indonesia creates its corporate value through financial policy or accounting policy by examining the effect of capital structure, dividends, and earnings management on corporate value. The influence of capital structure on company value is based on optimal capital structure theory. This theory suggested that an appropriate mix of debt and equity will create an optimal capital structure that will increase the value of the company (Modigliani & Miller [27]; Miller & Modigliani [26]; Myers, [28]). Lundstrum [25] also believed that optimal capital structure would maximize the value of the company based on the theory of optimal capital. This theory becomes the foundation that capital structure can be a tool to increase company value. The effect of dividends on company value is based on signaling theory. If the dividend payout can increase the value of the company, then it is considered as a positive signal by investors (Pinkowitz [31]). Conversely, if the dividend payout lowers the company value, it is considered a negative signal by investors. The effect of profit management on company value is based on informative profit management theory. Informative profit management will increase the value of the company (Scott [34]) because this management aims to communicate the true potential of the company to outside people. Capital structure, dividends, and profit management are empirically influenced by a set of investment opportunity. There are five main studies that examine the relationship between an investment opportunity set or IOS, capital structure, and dividends such as Smith and Watts [38], Gaver and Gaver [14], Abbot [1], Ho et al. [18], and Prasetyo [32] as it brought an Indonesian case. The relationship of the four variables in the study reflects the relationship between congenital factors (investment opportunity set) with financial decisions (capital structure and dividends). The first research which linked investment opportunity set or IOS with capital structure and dividends was Smith and Watts [38]. The results of their research showed that the larger the company, the greater the debt and the dividendyield. Besides, the greater the investment opportunity set, the lower the equity ratio or the higher the company's debt, the higher the ratio of dividend to share price. Furthermore, Gaver and Gaver [14] research classified the sample into a group of companies which grow and not grow. As a result, growing companies have lower debt ratio to equity and dividendyield than companies that do not grow. This result further specifies Smith and Watts [38] research for different sets of investment opportunities. Abbott [1] in the study has developed Smith and Watts [38] and Gaver and Gaver [14] research. The research examined the policy of capital structure and dividends in companies which undergo changes in investment opportunity set. The results showed that the most sensitive policy to change the investment opportunity set is the funding policy. Then, Ho et al. [18] continued the research of Gaver and Gaver [14] by adding the variable of leasing policies. It is explained that growing companies have lower debt ratio to equity and dividendyields. Those companies also finance their assets with leasing operations more than companies that do not grow. Ho et al. [18] also found that the ownership of shares by directors will weaken the relationship between investment opportunity set and company policies (capital structure, dividend, and leasing). In Indonesia, Prasetyo [32] replicated Gaver and Gaver [14] research. Prasetyo [32] shows that there is no significant difference between funding policies in growing and non-growth companies. Several studies also examined the effect of investment opportunity set on profit management. The research of Al Najjar and Belkaoui [2], Belkaoui [4], and Cheng et al. [9] revealed the effect of investment opportunity set on profit management. A set of investment opportunity through profit management is expected to increase the value of the company. This study examines the effect of investment opportunity set on capital structure, dividend, profit management, and company value to observe the consistency of results from previous studies. It is conducted with the same variable but with different time and object (in Indonesia) so that the consistency from previous studies will be known. Prasetyo [32] has indeed done a research with corporate objects in Indonesia but has not involved the variable of profit management and company value in the research model. In addition, this study also re-examined the effect of capital structure, dividend, and profit management on company value to provide empirical evidence of how company management creates its company value through financial policy or accounting policies or even both. Defond and Jiambalvo [11] and De Angelo et al. [12] proposed a research stating that companies that are problematic or in danger of bankruptcy often try to maintain the value of their companies through profit management for some time. Nevertheless, these studies are only casuistic in problematic and undeveloped companies to test the effect of capital structure on profit management. Based on these indications, this study will also examine the effect of capital structure on profit management. Profit management is the use of instruction or management policy in financial statement and transaction structure (Healy & Wahlen [17]). There is still a debate about the role of profit management within a company. Some say that profit management is purely opportunistic and is a cheating from the corporate manager. The financial statements will affect the outcomes of contracts based on accounting figures and will even be misleading to some stakeholders on the basis of company's economic performance (Healy & Wahlen [17]). Profit management, on the one hand, is considered informative because the management does profit management to underline the company's true long-term prospects and not just short-term performance. This profit management reports high accruals at a low profit and lower accruals at a higher profit so that profits tend to be steady from time to time. Informative profit management is shown by profits that tend to be stable from year to year without showing any significant fluctuations. Jiraporn et al. [21] indicated that there is an informative profit management that can increase the value of the company. The measurement of profit management has also not been agreed upon because the proof of profit management is external. Management will not acknowledge it unless it has been legally proven that its behavior has inflicted a financial loss to the company through profit management. There are two groups of well-known profit management measurements, namely the accrual basis and real-earning management activities (Tucker & Zarowin [36]). If the accrual basis group states that profit management is done after the financial reporting stage, real earning management activities group points out that profit management is planned before the company's operations even begin. Based on the discussion above, there are two different results from previous research that can be a gap for this research. First, with the assumption that the management objective is to maximize the value of the company, it cannot be concluded whether the management doing it through financial policies that are operational or through accounting policies in the form of profit management or both. If the management tries to influence company value through profit management, it needs to be tested whether the management is opportunistic or informative. Secondly, there are many proxies for the measurement of profit management but it is not yet agreed on which proxy that produces the best measurement. There are three main originalities proposed by the researchers. First, the researchers want to test whether the variable of capital structure influence the profit management or not because the research from Defond and Jiambalvo [11], De Angelo et al. [12], and Cheng and Liu [8] wrote that companies which are troubled by the capital structure and debt contracts tend to do a profit management to avoid sanction from creditors and regulators. Based on this issue, it can be said that the condition of the company's capital structure can lead to the emergence of profit management in order to increase the value of the company. Second, the researchers want to test whether the profit management is opportunistic or informative. If company value is created through the maximization of inherent factors in the form of characteristics, a set of investment opportunity and operational policies such as dividends and capital structure, the opportunistic issues of managers will be eliminated. However, if the company is indicated to do a profit management, it is necessary to analyze whether the profit management is opportunistic or informative. Then, this study will use either the accrual basis profit management or real earning management activities. It is known that previous research has not integrated the two observed variables as profit management indicators. This research is basically an extended replication of previous research. There are four things that distinguish this research from which. First, different time periods and objects. Second, instead of partial testing, the researchers use integrated testing. Third, the variable measurement indicator is not entirely the same as the previous research. Fourth, add the path of the influence of capital structure to profit management as a new invention. Based on this background, the purpose of the research is to examine the effect of investment opportunity sets on capital structure, dividend, profit management, and its impact on company value.

2 Conceptual Framework and Hypothesis

The agent's primary job is to maximize company value. The agency theory shows that there is a conflict between the principal and the agent because both are assumed to maximize the personal interest (utility maximizer) so that the agent not always acts on behalf with the principal. Based on the agency theory, there are two main opinions in concern to the benefit of maximizing company value such as for shareholders and for managers (Grossman & Stiglitz [15]). First, shareholders will require the company's management to work hard and do everything to maximize the value of its shares. Increasing shareholder value can be pursued by increasing profits through investment only on projects that will generate a large rate of return for the company. Shareholders also demand companies to be as efficient as possible by reducing costs such as production costs, raw materials, and labor for greater profits. The subsequent shareholders demand to share this large profit in the form of dividends. Second, it is assumed that maximizing company value should be part of the manager. Managers feel that company's profits are the result of their hard work so that it is right for them to receive the largest share of the profits. If the shareholder of the company believes otherwise, the manager will act opportunistically to maximize its utility. Opportunistic acts are often associated with bonus contracts. Initially, the bonus contract was created by the shareholder as a principal to motivate the rational agent to act on behalf of the principal when the agent's interest is in contrast with the principal's wish (Scott [33]). Performance-based bonuses are the largest share of total executive earnings. Performance is measured by accounting figures that can be managed opportunistically by the executive to maximize their bonus earnings. This agency conflict not only happens between shareholders and company management but also between creditors and corporate management. Management often prefers the source of funding in the form of debt compared to issuing new shares to avoid any new shareholders wishing to be involved in management decisions related to the company. More shareholders will produce greater demands of dividend payout if the company makes a profit. Therefore, the creditor is assumed to be more profitable for management because it is not involved in the company's operations and the expected return on interest does not follow the amount of profit as dividends. Nevertheless, creditors have an effective supervision mechanism for management performance (De Angelo et al. [12]). This supervision is mandatory to maintain the ratios in its financial statements on a certain minimum threshold. If it is failed to be met by the management, this will enable creditors to withdraw their funding from the company. Management efforts in maintaining these financial ratios will have an impact on the creation of company value, especially through accounting policies. Company value can be a built-in factor in the company. These inherent factors include a set of investment opportunity. Besides being an inherent factor, the value of the company can also be enhanced through the company's management policy. In increasing the value of the company, company's management policy can be in the form of a financial policy that affects the company's operations and accounting policies which only influence the company's financial statements. Financial policy is obtained through capital structure and dividend. Meanwhile, accounting policy is constructed by profit management. There are two types of theories that form the basis of hypotheses formulation in this study, namely the main theory and supporting theory. The main theory in this study is agency theory, which is the basis that the main task of the agent is to maximize the value of the company. Consequently, there are eight supporting theories in this study: size theory, power theory, signaling theory, informative profit management theory, opportunistic profit management theory, optimal capital structure theory, pecking order theory, and debt covenant theory. The theory of size indicates that larger companies have more complex problems which require supervision mechanisms from both external and internal complex companies to overcome the problems (Smith & Watts [38]). A large company is considered to have good future prospects seen from the investment opportunity set. The size of the company indicates the magnitude of risk so that managers need more consideration and expertise in decision making related to funding and corporate dividends. The complexity of this management also demands a great compensation to optimize its performance while minimizing opportunistic behavior and risk aversion (Lewellen et al. [24]). Power theory emphasizes that the directors have the greatest power in controlling the company thus they can make all decisions both on capital structure and dividend which will affect the value of the company (Scott [34]). This power should be enormous when the executive also acts as a shareholder. This study also specifically uses the measurement of management ownership in the operationalization of variables so that this power theory deserves to be the basis of empirical testing. The power of the shareholder which also part of the management may be reduced if there is a non-management shareholder that has a high bargaining value such as an institutional shareholder. The influence of institutional shareholder will be greater if the institution is related to the activities of the company as suppliers, customers, or are in the same industry. Furthermore, signaling theory is a sign that raises the company condition based on the perspectives of the people outside the company (Bhushan [5]). The presence of a signal will make investors interested in the company. The signal will be analyzed further by analysts before the investors make a decision to sell or buy company's shares. If there is a positive signal, investors will be interested to buy the share, so the market value increases; otherwise, when the signal is negative, investors will release the shares. If there are more investors who want to buy the shares of the company, the price of the shares will be higher so that the value of the company increased. Conversely, if there are few investors who interested in buying the shares, the price will decrease thus the value of the company also dropped. Smith and Watts [38] suggested that investment opportunity set, capital structure, and dividends are a type of signal caught by the market. One of the components which affects shareholders and managers' prosperity is the increase and decrease in company value. Profit management is the use of instruction or management policy in financial statement and transaction structure (Healy & Wahlen [17]). The financial statements will affect the outcomes of contracts based on accounting figures. These figures could be misleading to some users of financial statements on the basis of company's economic performance (Healy & Wahlen [17]). It is considered that the good profit management is the informative profit management. Company's management performs profit management to underline the company's true long-term prospects and not just short-term performance. Jiraporn et al. [21] indicated that there is an informative profit management that can increase the value of the company. When a profit management has a negative effect on company value, then the theory used in the company is certainly opportunistic profit management theory. The optimal capital structure theory says that the optimal capital structure is the one which can maximize the value of the company (Lundstrum [25]). This theory becomes the foundation that capital structure can be a tool to increase company value. Pecking order theory explains the sequence of funding. It is assumed that the financial manager does not take the optimal level of debt into account. Funding needs to be determined by investment needs. Pecking order theory can explain why companies that have a high-profit rate can have a small debt level. The debt covenant theory is part of the agency theory associated with the relationship between the company and its creditors. The agency theory points out that accounting figures are essential to maintaininga good relationship between company management and its creditors (De Angelo et al. [12]). Any form of financing in the capital structure gives certain requirements to the company. Typically, corporate creditors bind the management to a certain minimum limit or debt covenant (Watts & Zimmerman [40]). If a required ratio cannot be met through operational financial policy but the company still has the ability to repay the debt and is confident that in the subsequent period it can immediately reach the specified ratio requirement, the management will perform profit management to increase the profit so that it can fulfill the debt. Besidestesting the effect investment opportunities set on the capital structure, dividend, profit management, and the value of the company, this study will also examine the effect of capital structure, dividend, and profit management to company value and to observe the effect of capital structure on profit management. The issue of this research is about how a company management in Indonesia creates company value whether through the maximization of inherent factors in the form of investment opportunity set, or through financial policy such as capital structure and dividend, or through accounting policy that only influential in financial report but has no real impact for the company. If the company value is created through the maximization of inherent factors in the form of an investment opportunity set and financial policies such as dividends and capital structure, the opportunistic issues of managers are eliminated. However, if the company is indicated to conduct profit management, it is necessary to analyze whether the profit management of the company is informative or to create company value. Smith and Watts [38], Gaver and Gaver [14], Prasetyo [32], Abbot [1], and Ho et al. [18] revealed the effect of investment opportunity sets on capital structure and dividends. This research develops all of the five research above by adding the endogenous variable of profit management and company value. This investment opportunity set will be tested on capital structure, dividends, profit management, and company value. The effect of investment opportunity set on capital structure and dividends is based on signaling theory developed from the asymmetric information model of Myers and Majluf [29]. The bigger the investment opportunity set, the greater the debt and dividends of the company because creditors and investors consider it a positive signal (Smith & Watts [38]). The greater the reaction to a signal that reflects the expectation of market participants, the larger the amount of asymmetric information. Gaver and Gaver [14] concluded that a high investment opportunity set is a signal that there are greater risks facing the company so that management will require a larger fee to manage the company optimally and shareholders will demand a greater rate of return to inculcate its capital in the company. The effect of investment opportunity set on profit management is based on signaling theory. A high investment opportunity set should be a positive signal for the market that can ultimately increase the value of the company. However, investors sometimes become unaware. In order to make the investment opportunity set recognized by investors, the company can clarify it through profit management. The investment opportunity set itself is actually an inherent corporate factor that can be utilized as well as a signal to increase the value of the company. The capital structure will be tested for its impact on profit management and company value. The basic effect of capital structure on profit management is agency theory. The agency theory explains that accounting figures are essential for maintaining good relationships between company management and its creditors (De Angelo et al. [12]). Corporate creditors typically bind the management to a certain extent or Debt Covenant (Watt and Zimmerman, 1986). If a ratio cannot be met by operational policy while the company still has the ability to repay the debt and is confident that in the subsequent period it can immediately reach the specified ratio requirement, the management will perform profit management to increase the profit so that it can fill the debt. Lundstrum [25] also expressed that the influence of capital structure on company value is based on optimal capital structure theory. This theory suggested that the optimal capital structure is the one which can maximize the value of the company. The conflict of the agents occurs in capital structure decisions because besides to raise the shareholder value, managers also have an obligation to maintain the value of the company on a contractual basis with the creditors. The dividends will be tested for its impact on the value of the company. The test itself is based on signaling theory. The signaling theory becomes the basis that the dividend payout will show if the company is fundamentally profitable and has an increasing value. The willingness of management to pay dividends can reduce agency costs to ensure the managers who are going to increase the wealth of the shareholder, one of which through dividend payouts. Profit management is also tested for its impact on company value. Initially, profit management talks about the difference in utility between the principal and the agent. The basis of this concern is the theory of opportunistic and informative profit management (Siregar & Utama [37]). If the profit management is performed to increase the value of the company, then it belongs to the informative category. Meanwhile, if the value of the company becomes lower, then it is categorized as an opportunistic profit management. Overall, there are nine theories that underlie the relationship of the six variables in this study. The theories are agency theory, measure theory, power theory, signaling theory, informative profit management theory, opportunistic profit management theory, optimal capital structure theory, pecking order theory, and debt covenant theory. Based on the conceptual framework above, the conceptual model of this study will be described in subsequent chapters. Based on previous conceptual models of previous studies and arguments, this study aims to continue the research of Smith and Watts [38], Gaver and Gaver [14], Prasetyo [32], Abbott [1], and Ho et al. [18] on the effect of investment opportunity set on capital structure and dividends. However, due to the theoretical and empirical findings, this research will make the research model in the form of investment opportunity set which affects the capital structure, dividend, profit management, and company value. The conceptual framework of the complete research model can be seen in Figure 1 below.

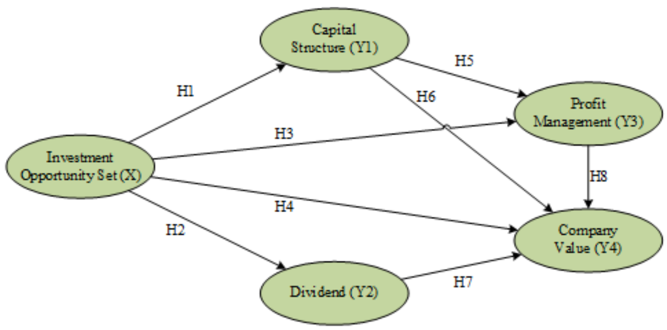

Figure1. *Conceptual Research Framework*

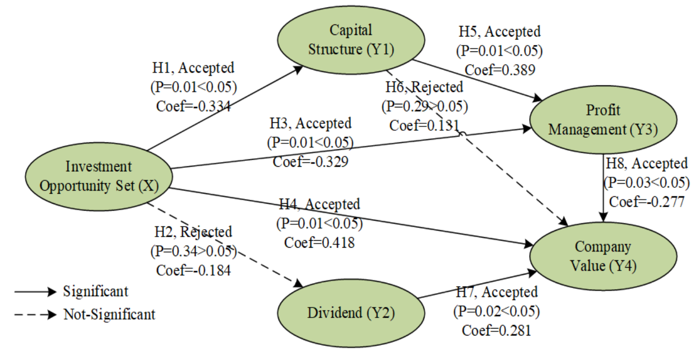

Figure2. *Research Finding Model*

The investment opportunity set is measured by using Depreciation Ratios per Value (Rasio Depresiasi per Nilai or DN), Asset Growth (Pertumbuhan Aktiva or PA), and Additional Capital per Value (Tambahan Modal per Nilai or TMN). The capital structure is measured by using the debt book value or equity and the debt market value/equity. Dividends are measured by using DPS (dividend per share), parliament (dividend payout ratio), and dividend yield (earning per share). Profit management is measured by using discretionary accrual (DA), abnormal discretionary load (ADL), and abnormal production costs (APC). Lastly, the company's value is measured by Tobin Q (market value of assets/net book value), market value per share (hargapasar per lembarsaham or HPLS), and the stock market price/ earnings per share).

3 Research Methods

The type of this research is explanatory research because researchers explain the causal relationship between the variables through hypothesis testing. This study is also an archival research which uses historical data and information from other archives (Bordens & Abbott [6]). The population in this study is a manufacturing company listed on Indonesia Stock Exchange within the period of 2005-2015. The sampling method used in this study is purposive sampling that the samples are taken based on certain criteria. Purposive sampling was used because the research purposes can only be achieved if it uses a manufacturing company that meets the criteria, such as (1) registered on the Indonesia Stock Exchange from 2005 to 2015, (2) publish financial statements, and (3) at least, has done a dividend payout during 2005 to 2015. The research samples are known to be 45 companies in 10 years so that there are 450 research data.

4 Results and Discussion

Overall, there are seven paths in the test results. The relationship between the results of this study can be seen in Figure 2 below. Furthermore, this study has 8 hypotheses. There are five accepted hypotheses and the rest are rejected (p-value <0.05 which indicates that the hypothesis is accepted).

4.1 The Effect of Investment Opportunity Set on Capital Structure

The hypothesis 1 which states that investment opportunity set has a significant effect on capital structure is accepted. The direction of the investment opportunity set on the capital structure is negative which means the smaller the depreciation per value, the greater the asset growth. Besides that, the smaller the additional capital per value, the lower the debt book value per equity as well as the market value of debt per equity and leverage. This result does not support the optimal capital structure theory but supports the pecking order theory as well as earlier empirical research. The theory that corresponds to the existence of a negative and significant influence of investment opportunity set on capital structure is pecking order theory. Pecking order theory was first proposed by Myers and Majluf [29]. In this theory, there is no optimal capital structure. Specifically, the company has a sequence of preferences (hierarchy) in the use of funds. It can be concluded that there are three conditions that are met for the validity of pecking order theory. First, a good investment opportunity set (high corporate asset growth, depreciation cost per small value, and additional capital per small value) will allow the company to have internal funds to invest. Second, a management which has more information than the investors and creditors of the company and does not want to give the signal to outside users. The use of internal funds makes certain investments more unobservable by outsiders such as competitors compared to the use of external funds such as issuing receivables. Thirdly, managers who are aware with the opportunity to have an advantageous investment and are able to fund the company by themselves prefer to enjoy their own profit and do not want to share with external parties such as creditors through interest and shareholders through dividends. This result is also in accordance with previous research. The effect of investment opportunity set on capital structure has been empirically verified by several studies such as from Smith and Watts [38], Gaver and Gaver [14], Prasetyo [32], Abbott [1], and Ho et al. [18].

4.2 The Effect of Investment Opportunity Set on Dividend

Hypothesis 2 which states that investment opportunity significantly influenced the dividend is rejected. The direction of the investment opportunity set on the dividend is negative. This negative direction of influence means that the smaller the depreciation per value, the greater the asset growth, and the smaller the additional capital per value, the less dividend per share, the dividend payout ratio, and the dividend yield. These results are inconsistent with previous theories and research that form the basis of hypothesis formulation. The results of this study are in contrast with the signaling theory. The effect of the investment opportunity set on the dividend is based on the signaling theory developed from the asymmetric information model of Myers and Majluf [29]. The bigger the investment opportunity set, the bigger the company's dividend because the creditor and the investor consider it as a positive signal (Smith & Watts [38]). Companies that have high investment opportunity set need a lot of money to make it into a real investment (as for an example, building a new factory). This company's investment can cause the company to have a small amount of cash so that there is a few money left for the dividend payouts. Outsiders prefer to see real signals (dividend payouts) as opposed to theoretical signals (the size of the investment opportunity set in the financial statements). Therefore, the size of the dividend is the factor which significantly affects the company value (the result of hypothesis 7) and is not investment opportunity set which is a long-term signal of the company. The results are also incompatible with previous empirical studies. The effect of investment opportunity set on dividend has been empirically verified by several studies such as Smith and Watts [38], Gaver and Gaver [14], Prasetyo [32], Abbott [1], and Ho et al. [18].

4.3 The Effect of Investment Opportunity Set on Profit Management

Hypothesis 3 which proposed that investment opportunity set has a significant impact on earning management is accepted. The direction of the investment opportunity set on profit management is known to be negative which means that the smaller the depreciation per value, the greater the asset growth, and the smaller the additional capital per value, the lower the discretionary accrual. In addition, the higher the abnormal discretionary burden, the lower the abnormal production cost. The direction of this negative influence shows that profit management has a special role as a balancer of information signals that management expects to convey to outsiders. When the investment opportunity set is low (the greater the depreciation per value, the smaller the asset growth, and the greater the additional capital per value) the company tends to perform profit improvement (high discretionary accruals, low abnormal discretionary loads, and high abnormal production costs). These results are in accordance with the signaling theory. Because a lot of information about the company is circulating in the public and investors often not focused, they cannot see the benefits of the company. To make this company's advantages become more visible, managers will use their discretionary to communicate their confident based on information they have as insiders (private information) on future earnings prospects (Tucker & Zarowin [36]). Investment opportunity set may look unfavorable in numbers, but when management believes that the company's prospects are good enough, management will send a positive signal to the market through profit management that improves the profits. When there is high investment opportunity set (the lower the depreciation per value, the greater the asset growth, and the smaller the additional capital per value) the company tends to perform earnings-type profit management (low discretionary accruals, high abnormal discretionary loads, and low abnormal production costs). This is in accordance with the theory of size. The theory of size shows that the larger the company, one of which can be seen through a good investment opportunity set, the more complex the problems encountered (Smith & Watts [38]). This is because large companies will make many stakeholders intervene in the company. The complex problems might be in the form that investors demand large dividends, the government asks for big profits, employees ask for a raise, and the demand to keep attracting competitors to enter the industry with big investment opportunity set. Through profit management that lowers the profits, the attractiveness of investment opportunity set for stakeholders that can inflict a financial loss of the company can be minimized. This result is consistent with previous studies. The effect of investment opportunity set on profit management has been empirically verified by the research from Al-Najjar and Belkaoui [2], Belkaoui [4], and Cheng et al. [9].

4.4 The Effect of Investment Opportunity Set on Company value

Hypothesis 4 which states that the set of investment opportunities have a significant effect on the value of the company is accepted. The direction of the investment opportunity set on the company value is positive. This means that the smaller the depreciation per value, the greater the asset growth, and the smaller the additional capital per value, the greater the Tobin q, and lastly, the greater the market price per share, the smaller the price to profit ratio. This result is in accordance with the theory and the results of previous research that became the basis of hypothesis in this study. The corresponding theory suggested that there is an effect of the investment opportunity set on company value, the agency theory, and the signaling theory. Based on the agency theory, the management will maximize the value of the company to its shareholders (Jensen & Meckling [20]) in which this can be accomplished by realizing the investment opportunity set into real growth (Ehie & Olibe [13]). The investment opportunity set of the company has become one of the inherent factors that can be utilized to increase the value of the company through a signaling mechanism. Several previous empirical research are in accordance with this result such as the research from Cho [10] and Ehie and Olibe [13].

4.5 The Effect of Capital Structure on Profit Management

The hypothesis 5 which states that the capital structure has a significant effect on profit management is accepted. The direction of the influence of capital structure on profit management is positive. This means that the greater the debt book value per equity and the debt market value per equity as well as the leverage, the greater the discretionary accrual. Besides that, the less the abnormal discretionary burden, the greater the cost of abnormal production. These results are new findings in this study. This result is in accordance with debt covenant theory as part of the agency theory of corporate relations with its creditors. The agency theory states that accounting figures are essential in maintaining a good relationship between company management and its creditors (De Angelo et al. [12]). Any form of financing in the capital structure gives certain requirements to the company. Corporate creditors typically bind management to a certain minimum limit or debt covenant (Watts & Zimmerman [40]). If a required ratio cannot be met through operational financial policy but the company still has the ability to repay the debt and is confident that in the subsequent period it can immediately reach the required ratio requirement, the management will perform a profit management to increase earnings so that it can be used to fulfill the debt.

4.6 The Effect of Capital Structure on Company value

Hypothesis 6 which states that the capital structure has a significant effect on the value of the company is rejected. The direction of the influence of capital structure on company value is positive. This means that the greater the debt book value per equity, the debt market value per equity, and leverage, the greater the Tobin q. Moreover, the larger the market price per share, the smaller the price to earnings per share ratio. This is not in accordance with the theory and the results of previous research that became the basis of hypothesis in this study. This hypothesis is rejected because it only observes the direct effect of capital structure on company value. However, based on observations of the indirect effect, this hypothesis is accepted. A discussion of indirect effects can be seen in the new findings section of the study. This result is inconsistent with agency theory and optimal capital structure. First, based on agency theory, a conflict occurs between the creditor and the company management. Company's management who decides to use funding sources in the form of debt will get additional supervision from creditors (De Angelo et al. [12]). This supervision is mandatory to maintain the ratios in its financial statements to a certain minimum threshold. If it fails to be met, the management will enable creditors to withdraw funding from the company. The efforts of the management in maintaining these financial ratios will have an impact on the creation of company value. Second, the theory of optimal capital structure proposed that the optimal capital structure maximizes the value of the company (Lundstrum [25]). Some theories suggest that there is an influence of capital structure on company value. Based on agency theory, management will maximize the value of the company for its shareholders (Jensen & Meckling [20]). One way to increase company value is through the creation of an optimal capital structure (Lundstrum [25]). This result is not in accordance with previous research. The influence of capital structure on company value has been empirically proven by several studies which were conducted by Arif [3], Iturriaga and Crisostomo [19], and Cheng et al. [9].

4.7 The Effect of Dividends on Company value

Hypothesis 7 which states that the dividend has a significant effect on the value of the company is accepted. The direction of this influence is positive which means that the larger the dividend per share, dividend payout ratio, and dividend yield, the bigger the Tobinq, and the larger the market price per share, the smaller the price to earnings ratio. This result is in accordance with previous theories and research that form the basis of this hypothesis formulation. The appropriate theories for this hypothesis are agency theory and signaling theory. First, according to the agency theory, it should be within the company that there is a separation between the owner as the principal and the management as the agent. The purpose of management is to maximize shareholder value. One proof that management could maximize company value is its ability and willingness to share dividends for its shareholders (Stevens & Jose [35]). Second, the signaling theory becomes the basis that the dividend payout is able to prove that the company is fundamentally profitable and has an increasing value (Brickley [7]). The willingness of management to pay dividends can reduce agency costs to ensure the managers who are going to increase the wealth of the shareholder, one of which through dividend payouts. This result is in accordance with previous research which has been empirically verified by Stevens and Jose [35], Pinkowitz [31], Iturriaga and Crisostomo [19].

4.8 The Effect of Profit Management on Company value

Hypothesis 8 which states that profit management has a significant effect on the value of the company is accepted. The direction of the profit management on the company value is negative which means that the greater the discretionary accrual, the smaller the abnormal discretionary burden, and the greater the abnormal production cost, the smaller the Tobin q, also that the smaller the market price per share, the greater the price to earnings ratio shares. The theory which underlies the negative influence of profit management on company value is the theory of opportunistic profit management. The theory that does not support the creation of company value through accounting policy is the theory of opportunistic profit management that the management makes accounting as a means to maximize its own profit rather than shareholder profits (Jiraporn et al. [21]). Profit management is almost always identified as opportunistic. Healy and Wahlen [17] believed that profit management occurs when managers use their valuation in financial statements and transaction structures to change financial statements or to mislead some shareholders on the basis of company's economic performance and to influence contract results based on the accounting figures reported. Subramanyam [39] added that opportunistic profit management diminishes company value in the long term.This result is in accordance with previous research such as the research from Tucker and Zarowin [36], Jiraporn et al. [21], and Kusumawardhani and Siregar [23].

6 Limitations, Suggestions and Research Recommendations

There are several limitations in this research, among others: (1) This research only uses manufacturing company as the object of observation, (2) This research uses an observation within the period of 2005 to 2009 which do not accommodate possible bias due to a global crisis. In 2008, there was a global crisis affecting the Indonesia Stock Exchange and its listed companies, (3) This study uses the figures in the financial statements so that it is strongly influenced by the applicable Financial Accounting Standards in Indonesia. In 2012, Indonesia's Financial Accounting Standards that is based on historical costs has changed its structure following the International Financial Reporting Standards or IFRS that is based on present value, especially in terms of assets. Based on the limitations of the study and the results obtained, it is suggested that: (1) Further research can develop observations with more diverse industries and compare it to each other. The benchmarking methodology of inter-industry profit management can be seen in Kothari et al. [22]; (2) Further research is recommended to observe within the period that accommodates the crisis (the pre-crisis period until 2008 and the post-crisis period in 2009 and above). These two periods can be compared to see the extent to which differences arise from the effects of the global crisis on capital markets in Indonesia; (3) It is recommended that subsequent research use post-observation periods of IFRS-based new accounting standards to see the impact of changes in accounting standards on fundamental conditions (financial statements) and company value especially for investors and creditors. There are several suggestions for investors, users of financial statements, and government as policymakers based on the discussion in this study. (1) Company's management is advised to use more financial action than accounting action. Sending a good signal about the company should use financial statements to increase the value of the company. Financial actions such as paying dividends are more easily responded by investors than accounting measures such as showing the size and growth of large companies, high investment opportunity set, large debts, and large profits in financial statements. Sending signals through passive actions are sometimes misunderstood by investors so that it may cause a decrease in company value (2) Investors are advised to not only see the amount of dividends as a basis of investing in a company but also fundamental factors such as company size and growth, management ownership, investment opportunity set, capital structure, and profit management to predict company value (3) The government as the policy maker should not only concerned on the final amount of the company's net profit presented in the financial statements but also need to be keen on profit management conducted by the company's management. If the government does not observe this phenomenon, the government can be difficult to bail out the private debt and would likely to bear the crisis due to the bankruptcy of companies which could have unexpected indications. This has occurred in the 1997 monetary crisis in Indonesia and in the 2008 global crisis in the United States and European countries.

ACKNOWLEDGMENT

This work was supported in part by the Department of Administrative Sciences, University of Brawijaya, Malang, Indonesia.

REFERENCES

[1] A. Abbot, Chaos of Disciplines, America: University of Chicago Press, 2001.
[2] F.K. Al Najjar & A. R. Belkaoui, "Empirical validation of a general model of growth opportunities," Managerial Finance, vol. 27, pp. 72-90., 2001.
[3] M. Arif, "Axiomatic Based Decomposition for Conceptual Product Design," Production Operations Management, vol. 14, no. 3, pp. 286-300, 2005.
[4] A. Belkaoui, "Intellectual capital and firm performance of US multinational firms: A study of the resource-based and stakeholder views," Journal of Intellectual Capital, vol. 4, no. 2, pp. 215-226, 2003.
[5] R, Bhushan, "Firm characteristics and analyst following," Journal of Accounting and Economics, vol. 11, no. 2-3, pp. 255-274, 1989.
[6] Bordens, & Abbott, Research Design and Methods: A Process Approach (7th ed.). New York: McGraw Hill., 2009.
[7] J.A. Brickley, "Shareholder wealth, information signaling and the specially designated dividend: An empirical study," Journal of Financial Economics, vol. 12, no. 2, pp. 187-209., 1983.
[8] J.F. Cheng & C.C. Liu, "A Study of management efficiency for internationalresort hotels in Taiwan," Journal of Accounting and Economics, vol. 15, pp. 139-146, 2008.
[9] Q. Cheng, S. Chen, X. Chen & T. Shevlin, "Are family firms more tax aggressive than non-family firms?," Journal of Financial Economics, vol. 95, no. 1, pp. 41-61, 2010.
[10] M. Cho, "Ownership structure, investment, and the corporate value: an empirical analysis," Journal of Financial Economics, vol. 47, no. 1, pp. 103-121, 1998.
[11] M.L. DeFond & J. Jiambalvo, "Debt covenant violation and manipulation of accruals," Journal of Accounting and Economics, vol. 17, no. 1-2, pp. 145-176, 1994.
[12] H. De Angelo, L. De Angelo, Skinner & J. Douglas, "Accounting choice in troubled companies," Journal of Accounting and Economics, vol. 17, no. 1-2, pp. 113-143, 1994.
[13] L. Ehie & K. Olibe, "The effect of R&D investment on firm value: An examination of US manufacturing and service industries," International Journal of Production Economics, vol. 128, pp. 127-135, 2010.
[14] J.J. Gaver & K.M Gaver, "Additional evidence on the association between the investment opportunity set and corporate financing, dividend, and compensation policies," Journal of Accounting and Economics, vol. 16, no. 1-3, pp. 125-160, 1993.
[15] S.J Grossman & J.E. Stiglitz, Information and Competitive Price Systems. America: Columbia University Academic Commons, 1977.
[16] S. Hadi, Conservation of Natural Resources and the Environment. Ecological approach to saving the earth, 1st printing. Yogyakarta: Gadjah Mada Universityy Press, 2012.
[17] P.M. Healy & J.M. Wahlen, "A Review of the Earnings Management Literature and Its Implications for Standard Setting," Accounting Horizons, vol. 13, no. 4, pp. 365-383, 1999.
[18] S.H. Ho, J. Huang, & B.C.Y. Lee, "Consumer attitude toward gray market goods," International Marketing Review, vol. 21, no. 6, pp. 598-614, 2004.
[19] F.J.L. Iturriaga & V.L. Crisostomo, "Do Leverage, Dividend Payout, and Ownership Concentration Influence Firms' Value Creation? An Analysis of Brazilian Firms," Emerging Market Finance and Trade, vol. 46, no. 3, pp. 80-94, 2010.
[20] M.C. Jensen & W. Meckling, "Theory of the Firm : Managerial Behaviour, Agency Costs and Ownership Structure," Journal of Financial Economics, vol. 3, pp. 305-360, 1976.
[21] P. Jiraporn, Y. Kim & W.N. Davidson, "Mutiple directorships and corporate diversification", Journal of Empirical Finance, vol. 15, no. 3, pp. 418-435, 2008.
[22] S.P. Kothari, A. Leone & C.E. Wasley, "Performance matched discretionary accrual measures," Journal of Accounting and Economics, vol. 39, no. 1, pp. 163-197, 2005.
[23] N.A. Kusumawardhani & S.V. Siregar, "Profit Management Phenomenon Approaching the IPO and its Relationship with the Initial Company Value and Post-IPO Company Performance: Empirical Study of IPO Companies in Indonesia in 2000-2003," Journal of the National Accounting Symposium XII, 2009.
[24] W. Lewellen, C. Loderer & K. Martin, "Executive compensation and executive incentive problems: An empirical analysis," Journal of Accounting and Economics, vol. 9, no. 3, pp. 287-310, 1987.
[25] L.L. Lundstrum, "Entrenched management, capital structure changes and firm value", Journal of Economics and Finance, vol. 33, no. 2, pp. 161-175, 2009.
[26] M.H. Miller & F. Modigliani, "Corporate Income Taxes and the cost of Capital: A correction," The American Economic Review, vol. 53, no. 3, pp. 433-443, 1963.
[27] F. Modigliani & M.H. Miller, "The Cost of Capital, Corporate Finance and Theory of Investment", The American Economic Review, vol. 48, no. 3, pp. 261-297, 1958.
[28] S.C. Myers, "Determinants of Corporate Borrowing," Journal of Financial Economics, vol. 5, pp. 147-175, 1977.
[29] S.C. Myers & N.S. Majluf, "Corporate financing and investment decisions when firms have information that investors do not

have", Journal of Financial Economics, vol. 13, no. 2, pp. 187-221, 1984.
[30] D. Noor, Introduction to Geology, Bogor: Pakuan University Press, 2012.
[31] L. Pinkowitz, "Does the Contribution of Corporate Cash Holdings and Dividends to Firm Value Depend on Governance? A cross-country analysis," Jounal of Finance, vol. 61, no. 6, pp. 2725-2751, 2006.
[32] I. Prasetyo, New Paradigm in Land Management in the Era of Regional Autonomy. Jakarta: Bappenas, 2000.
[33] A.J. Scott, "Rethinking human capital, creativity and urban growth", Journal of Economic Geography, vol. 9, no.2, pp. 147-167, 2009.
[34] D. Scott, "Developing country perceptions of high- and low-involvement products manufactured in other countries," International Journal of Emerging Markets, vol. 4, no.2, pp. 185-199, 2009.
[35] Stevens & Jose, "The Elevational Gradient in Altitudinal Range: An Extension of Rapoport's Latitudinal Rule", The American Naturalist, vol. 140, no. 6, pp. 893-911, 1992.
[36] J. Tucker & P. Zarowin, "Does Income Smoothing Improve Earnings Informativeness," The Accounting Review, vol. 1, pp. 251-270, 2006.
[37] S.V. Siregar & S. Utama, "Type of earnings management and the effect of ownership structure, firm size, and corporate-governance practices: Evidence from Indonesia", The International Journal of Accounting, vol. 43, no.1, pp. 1-27, 2008.
[38] C. Smith & R. Watts, "The investment opportunity set and corporate financing, dividend, and compensation policies," Journal of Financial Economics, vol. 32, no. 3, pp. 263-292, 1992.
[39] K.R. Subramanyam, "The pricing of discretionary accruals," Journal of Accounting and Economics, vol. 22, no. 1-3, pp. 249-281, 1996.
[40] R.S. Watts & J. Zimmerman, Positive Accounting Theory. Prentice-HallInc. (1986).