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Overconfidence and Size of Companies as a Predictor of Capital Structure and Company Values in Pharmaceutical Companies in Indonesia Stock Exchange

Ni Luh Eka Silvia Dewi[a]*, Ni Luh Putu Wiagustini[b]

[a,b]*Universitas Udayana, Denpasar, Bali-Indonesia*

[a]*Email: dewisilvia739@gmail.com*

[b]*Email: wiagustini@yahoo.com*

Abstract

The purpose of this study was to examine the overconfidence and firm size as a predictor of capital structure and firm value in companies listed on the Indonesia Stock Exchange during the period 2009-2016. This research is a causality research where there is a relationship between one or more variables. This study also does not directly link between predictor variables, namely for the capital structure of the firm's value. This study uses Path Analysis as a tool to analyze the relationships that occur. The location of the study was conducted at the Indonesia Stock Exchange at pharmaceutical companies by taking data through ICMD (Indonesian Capital Market Directory) for the period of 2009-2016. The results of the study found that excessive uncertainty significantly towards the capital structure. While the size of the company does not. The size of the company is significant to the value of the company. The test results of the capital structure on the firm's value are positive. Excessive self-confidence has a significant positive effect on the level of trust not insignificantly insignificant to the value of the company..

Keywords: Overconfidence; Size; Capital Structure; Capital Structure Theory; Company Value.

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* Corresponding author.

1. Introduction

Maximizing the value of a company is a financial management goal when a company is established. The company's financial performance can be seen through stock returns to see the benefits to be gained if investors invest in the company. One of the factors that can influence an increase in firm value is the capital structure. Capital structure is a balance between own capital and debt.

Companies with poor capital structure and very large debt will put a heavy burden on the company so that an optimal balance is needed in using these two sources so as to maximize the value of the company. This makes funding decisions very important because it will have an impact on the company's decision in determining the optimal capital structure. The funding decision is related to determining the amount of funding, where the funds come from, the amount of funds and the composition of the funds.

Trade-off theory explains that if the capital structure position is below the optimal point, any additional debt will increase the value of the company. One way to analyze the performance of a company is through the capital structure because the capital structure can reflect the good or bad of a company. The capital structure can also result in bankruptcy occurring so that it affects the company's activities. Trade-off theory explains if financing tends to use debt because debt will reduce the company's cost of capital so that an optimal capital structure will be determined.

Companies with a high level of capital structure show that the company has a large company size, with a high level of capital structure the company can expand outside the company so as to expand the size of companies that can compete in the capital market. The statement was evidenced from the research of [1,2,3,4,5], and research by [6].

Another factor that can influence the increase in firm value through stock prices is the size of the company. Firm size indicates that the larger the company, the greater the level of debt. The size of the company is considered able to influence the value of the company. The larger the size of the company, the easier it will be for companies to obtain funding sources both internal and external. So that companies can get more opportunities to get higher profits [7].

Empirical studies conducted by [8,9] show that the size of a company is strongly influenced by the decision to use debt in the company's capital structure, especially related to the company's ability to obtain loans. However, research conducted by [10] shows that large company size cannot guarantee that the value of the company is high.

Another factor that can affect the capital structure is the level of trust of managers. Not all managers act rationally (bound of rationality) because in financial decision making, managers have confidence above the average of the results of decisions taken. This belief has a cognitive bias or in economic phsychology referred to as overconfidence. Confidence in making funding decisions with either own capital or debt is necessary to assess that the investment is deemed feasible to do, but overconfidence will make investors overestimate the knowledge possessed by the investor itself, and underestimate the prediction done because investors overstate their capabilities [11]. Previous research conducted by [12] on the effect of overconfidence on firm value in manufacturing companies through the sales index shows insignificant results. Therefore, this research is carried out more specifically on pharmaceutical companies.

So far there are still few studies that consider the effect of overconfidence variables in the field of financial management, especially in the study of capital structure and investment. Research conducted by [13] shows that there is no clear evidence and enough ideas for confident managers tend to use high levels of debt. Other studies on overconfidence related to funding sources are also conducted by [14], that most tend to assume that the existence of debt as a source of funding is more a stimulator because it will spur to work more productively and discipline.

This research was conducted at pharmaceutical companies in the Indonesia Stock Exchange with the study period from 2009-2016. Pharmaceutical companies are chosen because they have the potential to continue to grow in the future. The growth of the national pharmaceutical market sales which for more than five years grew far above the national economic average growth.

2. Literature Review and Hypotheses

2.1 Trade-off theory

Trade-off Theory explains that if the capital structure position is below the optimal point then any additional debt will increase the value of the company, on the contrary if the position of the capital structure is above the optimal point then any additional debt will reduce the value of the company. If the assumption of an optimal capital structure target point has not been reached, then based on the trade-off theory predicts a positive relationship to the value of the company.

2.2 Pecking Order Theory

Pecking order explains why companies will determine the hierarchy of the most preferred source of funds. In this theory, companies tend to choose the use of funding sources that have the lowest risk first.

2.3 Firm Value

The main purpose of the company according to the theory of the firm is to maximize wealth or corporate value (value of the firm) [15]. Company value is a certain condition that has been achieved by a company as an illustration of public trust in the company after going through a process of activity for several years, namely since the company was established until now [16]. According to [17], the value of the company is the market value of the securities and equity of the company in circulation..

2.4 Capital Structure

Capital structure is the ratio or balance of the company's long-term funding as indicated by the comparison of long-term debt to equity [18]. According to [19] stated that "Capital structure theory tries to explain whether changes in the composition of funding will affect the value of the company if investment decisions and dividend policies are held constant". According to [20], capital structure is an important problem in making decisions about corporate finance. Capital structure decisions directly affect the amount of risk borne by shareholders and the expected rate of return or profit.

2.5 Company Size

According to [21] the size of the company can be interpreted as a measure of the size of the company seen from the value of equity, the value of sales, or the results of the total value of assets owned by the company. Company size (size) is the scale used in determining the size of a company. Companies that are large in scale usually tend to express more social responsibility than companies that have small scale [22].

2.6 Overconfidence

The phenomenon of overconfident is the tendency of decision makers to assess knowledge and information that is over-owned, beyond the actual reality that causes more errors. Overconfidence is a form of neglect of accurate information and support for biased information with high confidence [23]. When management overconfidence means there is a bias towards the real outcome.

2.7 Hypothesis

The conceptual framework of this study can be presented in Figure 1 below:

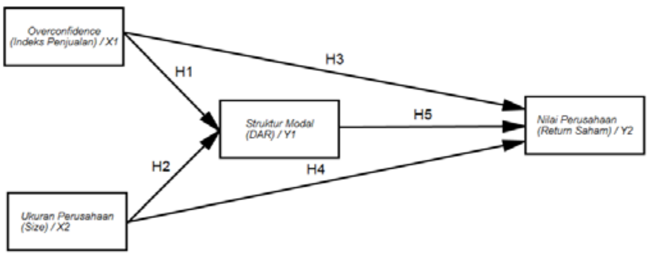

Figure 1: Research Framework

Based on the study of theorists and previous research that has been discussed, the research hypothesis is formulated as follows.

2.7.1 Effect of overconfidence on the capital structure

Research [24] found a positive relationship of overconfidence with debt levels. Study of [25,26] found that managers who are overconfident using more and cheaper long-term debt to reduce agency costs. The results of [27] found that confident managers prefer debt to equity. So that it was formulated:

H1: Overconfidence has a significant positive effect on the capital structure

2.7.2 Effect of company size on capital structure

Empirical studies conducted by [8,28,9] show that firm size has a significant positive effect on capital structure. [29] statistically shows a positive relationship between company size and capital structure. Study of [30] found that the use of long-term debt has a positive and significant effect among large-scale companies. Based on this, the following hypothesis is formulated.

H2: Firm size has a significant positive effect on capital structure

2.7.3 Effect of overconfidence on firm value

An empirical study conducted by [31] found that managers with overconfidence will be able to create corporate value. Research conducted by [32,33] shows that CEO's overconfidence has a significant positive effect on firm value. Based on this, the following hypothesis is formulated.

H3: Overconfidence has a significant positive effect on firm value

2.7.4 Effect of company size on company value

The empirical study conducted by [1,2,3], shows that the firm size variable has a positive and significant effect on firm value. Study of [5] found the highest positive impact on the value of the company is the size of the company. Research of [6] found a positive influence significantly on the size of the company on the value of the company as a major determinant of the value of the company. Based on this, the following hypothesis is formulated.

H4: Company size has a significant positive effect on company value

2.7.5 Effect of capital structure on firm value

Research conducted by [34] found that capital structure decisions have various implications and one of them affects the value of the company. Research conducted by [35] found that capital structure and firm value are one direction, the higher the capital structure, the higher the value of the company. Research conducted by [36,6,37,34] found a significant positive effect of capital structure on the value of the company as a major determinant of firm value. Based on this, the following hypothesis is formulated.

H5: Capital structure has a significant positive effect on firm value

3. Research Method

The location of the study was conducted at the Indonesia Stock Exchange at pharmaceutical companies by collecting data through the Indonesian Capital Market Directory (ICMD) by recording information on the company's complete financial statements during the period 2009-2016.

The variables used in this study are Overconfidence (X1), Company Size (X2), Capital Structure (Y1) and Company Value (Y2). Overconfidence is measured using the Sales Index. The Sales Index is a comparison between the sales index which is the base year with the actual year sales index. Sales Index can simply be formulated as follows:

$I_{t,0} = \frac{P_t}{P_0} \times 100\%.$

Information:

It, 0 = Sales index in year t with base year 0

Pt = Sales in year t

P0 = Sales in year 0

The size of the company proxied by using the natural logarithm of the total assets to calculate the size of the company, Size is stated in the following formula:

$$Size = Ln(Total\ Asset)$$

Capital structure is measured using DAR (Debt to Assets Ratio). Debt to Total Assets Ratio (DAR) is expressed in percentage units (%) and is calculated by the following formula:

$$DAR = \frac{Total\ Debt}{Total\ Asset} x100\%$$

The value of the company is the value of shareholder wealth at the Pharmaceutical company on the Indonesia Stock Exchange which is calculated by the Stock Return. Company value measured by assessing the level of stock returns formulated as follows:

$$R_{i} = \frac{Pt-(Pt-1)}{Pt-1}$$

Information:

Rit = The rate of profit of the period i shares t

Pit = The closing stock price i in period t

P 1 – i = closing stock price i in the previous period

The data used in this study are all secondary data, namely data that is not directly obtained from the company, but obtained in the form of data that has been collected, processed and published by other parties, namely the Indonesia Stock Exchange (IDX) in the form of data through the website www.idx .co.id and published www.yahoofinance.com.

The number of samples taken by conducting a census of 9 companies listed on the Indonesia Stock Exchange during the period 2009-2016. The analysis will be carried out by collecting data from the observation period which is 7 (seven) periods (2009-2016) so that the number of observations is 63 cases. The list of companies that are the research sample is presented in Table 1 as follows:

Table 1: Company Samples in Research

NO	CODE	COMPANY NAME
1.	DVLA	Darya Varia Laboratoria Tbk
2.	INAF	Indofarma Tbk
3.	KAEF	Kimia Farma Tbk
4.	KLBF	Kalbe Farma Tbk
5.	MERK	Merck Indonesia Tbk
6.	PYFA	Pyridam Farma Tbk
7.	SCPI	Merk Sharp Dohme Pharma Tbk
8.	SQBB	Taisho Pharmaceutical Indonesia Tbk
9.	TSPC	Tempo Scan Pacific Tbk

Source: ***Indonesian Capital Market Directory,*** **2015**

Data analysis techniques used in this study are Path Analysis using the SPSS (Stastical Product and Service Solutions) application program version 21. This technique is used to see the effect of overconfidence and firm size as a predictor of capital structure and firm value on pharmaceutical companies in the Indonesia Stock Exchange period 2009-2015. Path provides explicit causality between variables shown by arrows. Each value ρ describes the path and path coefficients formulated in the following equation:

$$Y1 = \alpha + \beta_1 X_1 + \beta_2 X_2 + e_1 \quad \text{.....} \quad (1)$$

$$Y2 = \alpha + \beta_3 X_1 + \beta_4 X_2 + \beta_5 Y_1 + e_2 \quad \text{.....} \quad (2)$$

Information:

X1 = Overconfidence

X2 = The Company size

Y1 = Capital Structure

Y2 = Corporate Value

α = contsanta

β1 = Path coefficient X1 and Y1

β2 = Path coefficient X2 and Y1

β3 = Path coefficients X1 and Y2

β4 = Path coefficient X2 and Y2

β5 = Path coefficients Y1 and Y2

e1 e2 = error.

4. Results

4.1 Descriptive Statistics

Descriptive statistical test results are intended to determine the characteristics of data distribution or image phenomena.

Table 2: Descriptive Statistics Test Results

Variable	**Minumum**	**Maksimum**	**Mean**	**Std.Dev**	**N**
Overconfidence	0,430	8,420	1,610	1,186	72
Size	25,330	30,350	27,830	1,037	72
Capital structure	0,150	1,030	0,385	1,194	72
Firm value	-0,010	0,050	0,044	0,016	72

Source: Data processed, 2018

Table 2 shows that the average value of manager overconfidence in pharmaceutical companies on the Indonesia Stock Exchange in 2009-2016 was 1.610 and the standard deviation was 1.185. The average value of overconfidence is greater than the standard deviation value so this shows good data distribution results. The company size variable has an average value of 27.8303 and a standard deviation of 1.03716, with an average value that is greater than the standard deviation, it can be concluded that the distribution of company size data is good.

Table 2 shows the average value of the structure with an average value of 0.3848 and a standard deviation of 1.19432. In the capital structure variable the average value of the data is smaller than the standard deviation so that this indicates a lack of data distribution good. The value of the company has an average value of 0.0436 with a standard deviation of 0.01613. The average value that is greater than the standard deviation is an indication that the results of the distribution of data variable value of the company is good.

4.2 Classic Assumption Test

Prior to data regression, it was previously tested using classic assumption tests. Descriptive statistical test results show the points spread near zero, so the data are said to be normally distributed with the results shown in Figure 2.

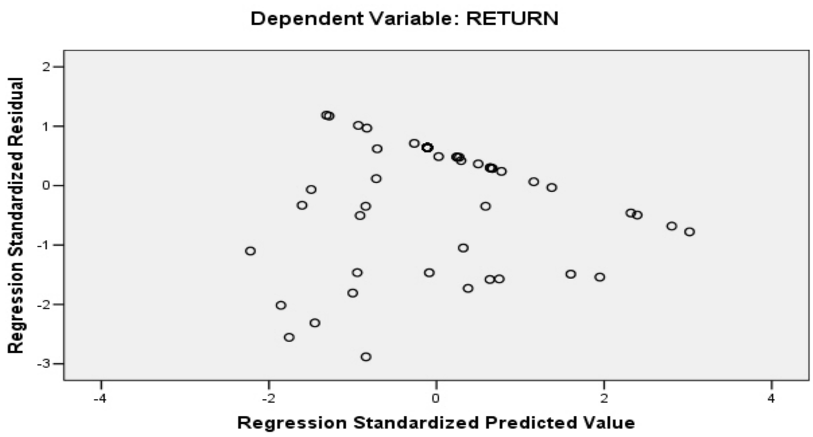

Figure 2: Histogram The results of descriptive statistics testing of Pharmaceutical Company data on the Indonesia Stock Exchange Period 2009-2016.

Multicollinearity test results show that the tolerant value is not more than 10 percent or VIF is less than 10, so there is no multicollinearity according to the results presented in table 3.

Table 3: Assumption of Multicollinearity Test Results

Model	Variable	VIF	Information
1	Overconfidence→Firm value	1,421	Non Multicollinearity
2	Size→ Firm value	1,126	Non Multicollinearity
3	Overconfidence→Capital Structure	1,025	Non Multicollinearity
4	Size → Capital Structure	1,025	Non Multicollinearity
5	Capital Structure → Firm value	1,435	Non Multicollinearity

Source: Data Processed, 2018

In the model there is no heteroscedasticity problem, where the increase in the value of the dependent variable is followed by an increase in the residual according to the results in Figure 3.

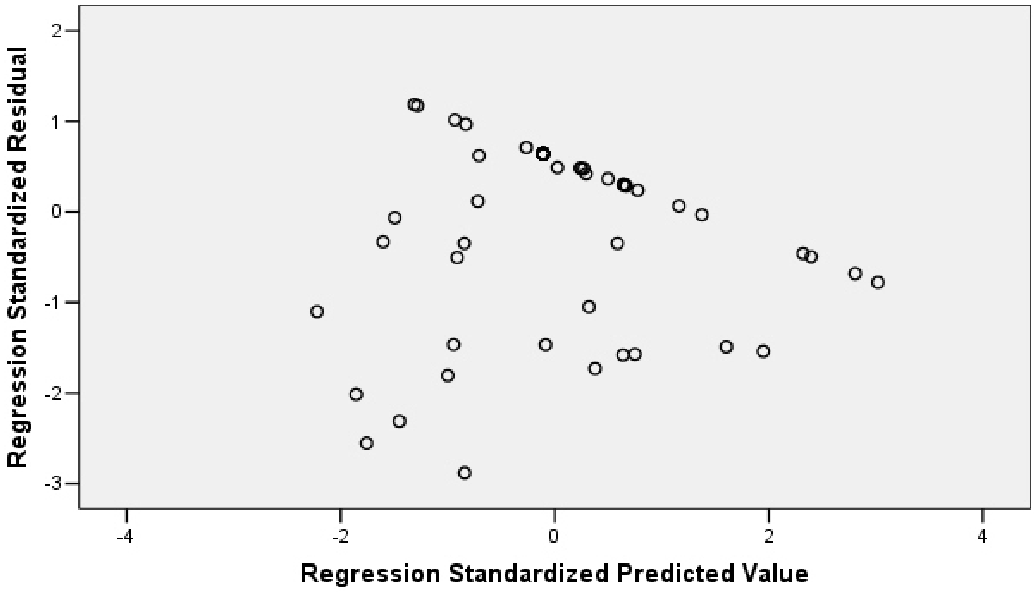

Figure 3: Scatterplot Heteroscedasticity test results of Pharmaceutical Company Data on the Indonesia Stock Exchange Period 2009-2016

4.3 Hypothesis Testing

The following is a summary of the results of the regression data processed from the path coefficient:

Table 4: Summary of Regression Analysis Results

<table>
<tr><th>Model</th><th>Variable</th><th>Regression Coefficient</th><th>Sig.t</th></tr>
<tr><td rowspan="3">Regression I

(Sales index and Size against DAR)</td><td>Overconfidence</td><td>0,525</td><td>0,000</td></tr>
<tr><td>Size</td><td>-0,266</td><td>0,011</td></tr>
<tr><td colspan="2">Contsanta</td><td>1,632</td></tr>
<tr><td rowspan="4">Regression II

(Sales index, Size, and DAR on stock returns)</td><td>Overconfidence</td><td>0,017</td><td>0,898</td></tr>
<tr><td>Size</td><td>0,265</td><td>0,026</td></tr>
<tr><td>Capital Structure</td><td>0,367</td><td>0,007</td></tr>
<tr><td colspan="2">Constanta</td><td>-1,627</td></tr>
</table>

Source: Data Processed, 2018

Based on Table 4, it can be explained that all the variables studied are the relationship of the overconfidence variable and company size to the capital structure, as well as the overconfidence and firm size of the firm value can be explained in the following figure below:

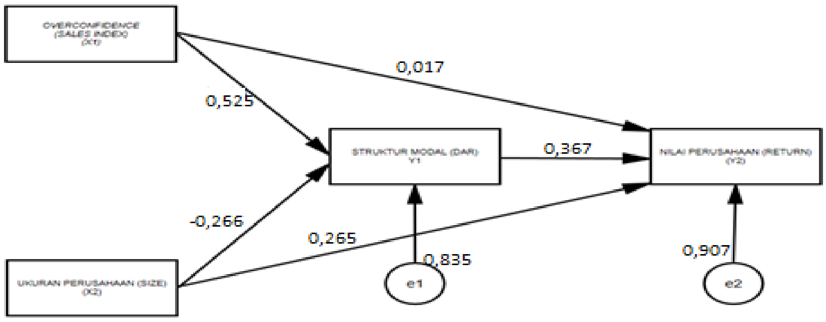

Figure 4: Path Coefficient of Overconfidence and Company Size as Predictors of Capital Structure and Firm Value at Pharmaceutical Companies on the Indonesia Stock Exchange

Path coefficient value obtained from the relationship between overconfidence variables and capital structure is 0.484 with a significance value of 0.000 which is less than α = 0.05. This means that the overconfidence variable has a significant positive effect on the capital structure of the pharmaceutical companies on the IDX. The hypothesis that overconfidence has a significant positive effect on proven capital structure.

Path coefficient value obtained from the relationship between company size variables and capital structure of -0.266 with a significance value of 0.011. This means that this means that the firm size variable has a significant negative effect on the capital structure of the pharmaceutical companies on the IDX. Every increase in the value of the company size by using Ln Total Assets, it will affect the decline in the company's capital structure. The hypothesis states that the size of the company has a significant positive effect on the capital structure is rejected.

The results show that the path coefficient value obtained from the relationship between the variable overconfidence and the company value is 0.017 with a significance value of 0.898. Although the regression coefficient shows a positive direction, the significance value of overconfidence is above the value of α = 0.05. This means that the variable overconfection does not have a significant effect on the value of the company in the pharmaceutical company on the IDX. So the third hypothesis is rejected.

Path coefficient value obtained from the relationship between company size variables with company value of 0.265 with a significance value of 0.026 which is below the value of α = 0.05. This means that the company size variable has a significant positive effect on the value of the company in the pharmaceutical company on the IDX. The hypothesis states that firm size has a significant positive effect on proven company value.

Path coefficient value obtained from the relationship between capital structure variables with firm value of 0.367 with a significance value below α = 0.05, namely 0.007. This means that the capital structure variable has a significant positive effect on the value of the company in the pharmaceutical companies on the IDX. The hypothesis states that the capital structure affects the proven value of the company.

With the results of testing the hypothesis that has been described so that it can be described the relationship of the research variables in Figure 5.

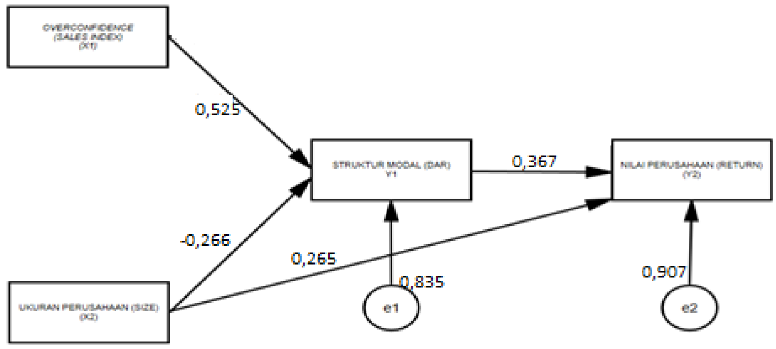

Figure 5: Path Coefficient of Overconfidence and Company Size as Predictors of Capital Structure and Firm Value at Pharmaceutical Companies on the Indonesia Stock Exchange

5. Discussions

5.1 Effect of Overconfidence on Capital Structure

The results of this study indicate that overconfidence has a significant positive effect on the capital structure. This shows that with a high level of confidence will affect the increase in capital structure. The results of this study are in accordance with the Signaling Theory on Capital Structure Theory, which is mentioned when managers have more information than outside parties called asymmetric information (asymmetric information), so that it will affect the optimal capital structure.

The results of this study are consistent with those conducted by [31] who found that capital structure is a function of overconfidence. This is confirmed by the results of research by [24] who found a positive relationship between overconfidence and debt levels. Managers who are overconfident use more and cheaper long-term debt to reduce agency costs [25].

5.2 Effect of Company Size on Capital Structure

The results of this study found that the size of the company had no significant positive effect on the capital structure but had a significant negative effect. The results of this study conflict with the research of [8,28,9]. In this study it was proved that the size of the company had a significant negative effect on the company's capital structure which was measured using Debt to Assets Ratio.

This research found things that were in line with [38] that the size of the company had a significant negative effect on the capital structure. This happens because companies that have high assets are able to maximize assets owned by placing cash held as the main operational source so as to reduce the amount of debt they have [38]. Furthermore, Reference [39] stated that this happened because the use of debt in large companies was connoted as a bad thing. As a result, large companies prefer to use their own capital from debt. Large-sized companies mean having a large total asset and internal funding sources as well, thus reducing funding through debt.

5.3 Effect of Overconfidence on Company Value

The results of this study found that overconfidence does not have a direct and significant effect on firm value. The results of this study are contrary to [31,29,32,33].

The results of this study are in line with [12] who found that overconfidence does not contribute to increasing the value of the company which means that the overconfidence measured by the sales index is not able to explain the variation in changes in the value of the company directly. The cause of the insignificance of the influence of overconfidence on firm value is related to information problems, namely the existence of asymmetric information between managers and outsiders.

5.4 Effect of Company Size on Company Value

The results of this study found that firm size had a significant positive effect on firm value. The size of the company determines the size of the company by getting a larger loan and larger funds can expand to a larger capital market so that the value of the company increases.

This research is in line with the study conducted by [1,2] which shows that firm size variables have a positive and significant effect on firm value. This was reinforced by [4] who stated that large companies can increase the value of manufacturing companies so that large company policies will have a greater influence on public interests than smaller companies.

5.5 Effect of capital structure on firm value

This study found that capital structure has a significant positive effect on firm value. The results of this study are in accordance with the Trade-off Theory which explains that if the capital structure position is below the optimal point then any additional debt will increase the value of the company, on the contrary if the capital structure position is above the optimal point then any additional debt will reduce the value of the company.

The results of this study support research conducted by [34,36,6,37,35] who found the capital structure and value of the company going in the same direction. Capital structure can increase and maximize the value of the company with good capital management to increase stock returns.

6. Conclusions

Based on the results of the research conducted and the discussion in the previous chapter, it can be concluded that Overconfidence has a significant positive effect on the capital structure. Company size has a significant negative effect on capital structure. Overconfidence has no direct and significant effect on company value. Company size has a significant positive effect on firm value. Capital Structure has a significant positive effect on firm value.

Based on the results of this study it is advisable for a company to remember that, in increasing the value of the company by using an optimal capital structure, certain levels of overconfidence are needed to improve the capital structure which can then maximize the value of the company with different levels of company size. In addition, issuers should use more long-term debt than equity capital in financing the company's operations because it has more impact on company value.

This research still has limitations in the overconfidence theory so that further research can be put back in several theories that are more relevant to the results of the study that are more supportive of the variables related to overconfidence. Subsequent research can also include gender variables to measure the level of manager's overconfidence so that there are differences in the results found with the level of overconfidence of male and female managers in maximizing the value of the company by using certain measuring instruments..

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