

The Effect of Financial Management and Investment Decision on Firm Value with Profitability as a Mediating Variable

Financial Management
and Investment
Decision

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Henny A. Manafe^{1*}, Tyahya Whisnu Hendratni², Subur Harahap³,
Ikramina Larasati Hazrati Havidz⁴

¹Department of Management, Faculty of Economics and Business, Universitas Katolik
Widya Mandira; Kupang, Indonesia

²Department of Economics Science, Faculty of Economics and Business, Universitas
Pancasila; Jakarta Selatan, Indonesia

³Department of Accounting, Faculty of Economics, Institut Bisnis Nusantara; Jakarta
Timur, Indonesia

⁴Department of Business Administration, Faculty of Business, Universitas Presiden;
Cikarang, Indonesia

*Corresponding Author E-Mail: hennyunwira@gmail.com

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ABSTRACT

Firm value reflects market perceptions of a company's performance and long-term sustainability. However, empirical evidence regarding the influence of financial management and investment decisions on firm value remains inconsistent, indicating that the underlying internal mechanisms are not fully understood. This study aims to examine the effects of financial management and investment decisions on firm value, incorporating profitability as a mediating variable for companies listed on the Indonesia Stock Exchange. A quantitative approach with a causal research design was employed, utilizing secondary data from annual financial statements covering the 2019–2023 period. Financial management and investment decisions were measured using financial structure and asset growth indicators, while profitability and firm value were assessed using profit performance ratios and market-based ratios. Data analysis was conducted through multiple linear regression, with mediation tested using the Sobel test. The results reveal that financial management and investment decisions do not consistently exert a direct effect on firm value but significantly influence it through enhanced profitability. These findings underscore the critical role of profitability as a mediating mechanism in value creation and provide practical implications for managers in formulating financial and investment policies that enhance profitability and long-term firm value.

Keywords: Financial Management, Firm Value, Investment Decisions, Profitability.

INTRODUCTION

Firm value is a key indicator that investors use to assess a company's performance, risk, and long-term sustainability prospects (Alsayegh et al., 2022). In the context of an increasingly integrated global market, increasing the value of a company is a strategic objective that is influenced by the effectiveness of financial policies and corporate investment decisions. Modern corporate financial studies confirm that managerial decisions regarding funding structures and investment allocations have direct implications for market perception and firm value (Rumasukun & Nochh, 2024). Therefore, a comprehensive understanding of the factors that determine a company's value is a crucial issue in contemporary corporate finance literature.

The development of corporate finance theory shows that a company's value is determined not only by financial decisions but also by the dynamic interaction among

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funding policies, investments, and operational performance (Gulaliyev & Huseynli, 2021). Signal theory and agency theory explain that a company's financial decisions serve as signals to the market regarding the company's future profit prospects and stability (Puzakov et al., 2024; Arhinful et al., 2025). In conditions of global economic uncertainty, investors are increasingly paying attention to the company's ability to convert financial policies into sustainable profit performance. This suggests that bridge ability has the potential to play an important role in bridging the relationship between managerial decisions and firm value.

In Indonesia, the capital market has experienced significant growth in line with the increase in the number of listed companies and the participation of domestic investors. However, fluctuations in the value of companies on the Indonesia Stock Exchange are still a frequent phenomenon, especially in companies that have aggressive financial structures and investment policies. Several empirical studies on Indonesian companies show that financial policies do not always directly increase a company's value (Hariyani et al., 2021; Utami, 2021). This condition indicates that there are other internal factors that affect the effectiveness of financial policies and investment decisions in creating firm value in the Indonesian capital market.

Several previous studies by Selfiani et al. (2023) have examined the influence of financial management and investment decisions on firm value, but the results still show inconsistencies. Studies by Hasanuddin (2021) have found a positive and significant influence between investment decisions and firm value, while other studies by Kontuš et al. (2023) reported weak or insignificant effects. These differences in results suggest that the relationship is not direct and is likely influenced by intermediate variables. Thus, there are still research gaps related to internal mechanisms that explain how financial and investment policies translate into increased firm value.

Profitability is often used as an indicator of financial performance, but its role as a mediating variable in the relationship between financial policy and corporate value has not been consistently explored, particularly in the context of emerging markets. Several studies have shown that profitability has a significant influence on firm value, but have not tested its function as a transmission mechanism for financial policy (Akash et al., 2023). Studies by D'Amato (2021) tend to treat profitability as an independent variable without considering the role of structural mediation. Therefore, research is needed that explicitly tests the link between profitability and the relationship between financial management, investment decisions, and firm value.

Based on the research gap, this study aims to analyze the influence of financial management and investment decisions on firm value by including profitability as a mediating variable. This study seeks to determine whether financial policies and investment decisions can increase the company's value directly or through increased profitability. This research was conducted on companies listed on the Indonesia Stock Exchange using annual financial statement data. Thus, this research is expected to provide a more comprehensive empirical understanding of the company's value creation mechanism.

This research makes a theoretical contribution by expanding the corporate finance literature through testing the role of profitability as a mediating variable in the relationship between financial management, investment decisions, and firm value. Conceptually, this study clarifies the internal mechanisms that link financial policy to market perception. Practically, the findings of this study have important implications for company management in formulating financial and investment policies aimed at improving profit performance. In addition, this study also provides a reference for investors in assessing the quality of a company's financial decisions as a basis for long-term investment decision-making.

LITERATURE REVIEW & HYPOTHESIS DEVELOPMENT

The Effect of Financial Management and Investment Decisions on Firm Value

Financial management constitutes a strategic function related to the management of a firm's funding structure, liquidity, and financial risk in order to maximize firm value (Siagian & Siagian, 2025). From the perspectives of agency theory and signaling theory, a firm's financial policy serves as a signal to investors regarding the firm's stability and future prospects. An optimal funding structure can reduce the cost of capital and enhance market confidence, thereby positively influencing firm value (Kontuš et al., 2023). However, several studies by Gennaro (2021) indicate that excessive reliance on debt may increase financial risk and ultimately reduce firm value, suggesting that the relationship between financial management and firm value remains context-dependent.

Investment decisions reflect a firm's policy in allocating funds to productive assets that are expected to generate future cash flows. Based on investment theory and firm growth theory, appropriate investment decisions can enhance production capacity, expand business opportunities, and support the sustainability of a firm's long-term performance. Therefore, investment decisions represent a critical factor in determining a firm's ability to create value for shareholders. Several empirical studies by Suriawinata et al. (2023) indicate that increases in capital expenditure and asset growth contribute to higher firm value, as such investments signal stronger growth prospects and business expansion potential. However, studies by Haidari (2023) suggest that investment decisions do not always receive a positive response from the market, particularly when they are not accompanied by adequate improvements in operational performance or when investors perceive the investments as highly risky.

H1: Financial management has a positive effect on firm value.

H2: Investment decisions have a positive effect on firm value.

The Effect of Financial Management and Investment Decisions on Profitability

Effective financial management plays a critical role in maintaining cost efficiency and optimizing the utilization of corporate resources. A balanced funding structure and sound liquidity management can enhance a firm's capacity to generate profits. Previous research has demonstrated that financial ratios reflecting financial management practices are significantly associated with a firm's level of profitability (Rashid, 2021; Ardini & Adhitya, 2022). Therefore, financial management is not only oriented toward capital structure decisions but also has direct implications for a firm's profit performance (Parulian & Siregar, 2025).

Investment decisions directed toward productive assets are expected to enhance operational efficiency, strengthen production capacity, and increase firm revenue. From the perspective of growth theory, effective investment serves as a primary driver of long-term profit growth and competitive advantage in the market (Fadillah et al., 2021; Pangestuti et al., 2022; Oyeyipo et al., 2023). Several studies by Putri and Suhartono (2022) and Sihombing et al. (2023) have found that asset growth and capital expenditure positively influence a firm's profitability. However, inefficient investments or those misaligned with a firm's capacity and strategic objectives may reduce investment returns and ultimately weaken profitability.

H3: Financial management has a positive effect on profitability.

H4: Investment decisions have a positive effect on profitability.

The Effect of Profitability on Firm Value

Profitability is a fundamental indicator of financial performance that reflects a company's ability to generate earnings from its assets and capital (Ardini & Adhitya, 2022). From the perspective of signaling theory, a high level of profitability provides a positive signal to the market regarding a company's prospects, financial stability, and long-term sustainability. Investors generally interpret strong profitability as evidence of

effective managerial performance and efficient resource utilization. Consequently, firms that demonstrate higher profitability tend to attract greater investor confidence and stronger market attention. Several empirical studies by Putri and Puspitasari (2022) and Bon and Hartoko (2022) have shown that profitability has a positive and significant effect on firm value because it strengthens investors' expectations of future returns and reduces perceived investment risk. Therefore, profitability plays a crucial role in shaping how the market evaluates a company's financial condition and growth potential.

Beyond serving as a performance indicator, profitability also functions as an important mechanism that links internal managerial decisions with external market valuation. A firm that consistently generates strong profits indicates that its operational strategies, financial policies, and investment decisions are implemented effectively. Higher profitability improves a firm's capacity to distribute dividends, reinvest in productive assets, and maintain financial stability. These conditions enhance market perceptions and support sustainable value creation. Accordingly, profitability can be regarded as a key factor that bridges internal corporate performance with market valuation, making it an important determinant in explaining variations in firm value across companies (Pangestuti et al., 2022).

H5: Profitability has a positive effect on firm value.

The Effect of Profitability as a Mediating Variable

The corporate finance literature indicates that the influence of financial policies and investment decisions on firm value is not always direct (Sumarno et al., 2023). Profitability has the potential to function as a transmission mechanism that explains how a firm's internal policies translate into increased market value. In this context, profitability reflects the effectiveness of managerial decisions in converting financial resources and investments into sustainable earnings (Ronald & Samuel, 2022). When financial and investment policies can improve profit performance, the market tends to respond positively because profitability signals stronger operational efficiency and future growth prospects. Consequently, profitability may serve as an important intermediary that links internal corporate decisions with external market valuation.

Several studies by Putri and Wiksuana (2021) and Asni and Agustia (2022) have begun to examine the mediating role of profitability and have found that this variable can strengthen the relationship between financial policies and firm value. These findings suggest that profitability not only acts as an indicator of financial performance but also plays a strategic role in transmitting the effects of managerial decisions to market outcomes. However, empirical studies by Damayanti and Sucipto (2022) that explicitly test the mediating role of profitability remain relatively limited, particularly in the context of companies operating in emerging markets such as Indonesia. Therefore, further research is necessary to provide deeper empirical evidence regarding how profitability functions as an intermediary mechanism in the relationship between financial management, investment decisions, and firm value.

H6: Profitability mediates the influence of financial management on firm value.

H7: Profitability mediates the influence of investment decisions on firm value.

Figure 1 illustrates the conceptual framework of the study that examines the relationships among financial management, investment decisions, profitability, and firm value. Financial management and investment decisions are hypothesized to influence firm value both directly and indirectly through profitability. In this framework, profitability acts as a mediating variable that links financial management and investment decisions to firm value. The solid lines represent the direct relationships among variables (H1–H5), while the dashed lines indicate the mediating relationships of profitability (H6–H7) in influencing firm value.

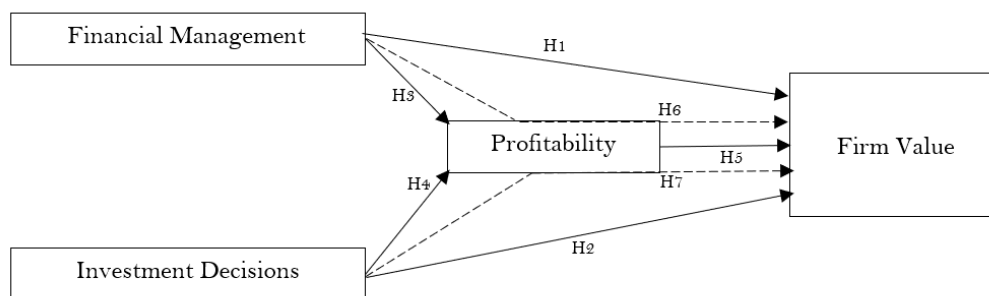


Figure 1. Conceptual Framework

RESEARCH METHODS

This study adopts a quantitative approach with a causal research design to examine the relationships among financial management, investment decisions, profitability, and firm value. A quantitative approach is employed as it enables the use of measurable financial indicators and statistical analysis to test hypotheses and explain relationships among variables objectively. Causal design facilitates the identification of direct and indirect effects between independent and dependent variables, particularly the mediating role of profitability in influencing firm value. The population consists of all companies listed on the Indonesia Stock Exchange during the 2019–2023 period, selected due to the availability of audited and publicly accessible financial statements. The sample is determined through purposive sampling based on criteria including continuous listing, complete financial reports, availability of relevant data, and absence of delisting. The unit of analysis is firm-year observations, representing each company across the five-year period.

This research utilizes secondary data obtained from annual financial statements and corporate reports published by the sampled companies. The data are collected from several reliable sources, including the official website of the Indonesia Stock Exchange, the annual reports of each company, and other relevant and credible supporting sources. These sources provide comprehensive financial information that enables accurate measurement and analysis of the research variables.

The variables in this study consist of independent variables, a mediating variable, and a dependent variable. The independent variables include financial management and investment decisions. Financial management reflects the firm's ability to manage its funding structure, liquidity, and financial risk, and is measured by financial ratios such as the debt-to-equity ratio, debt-to-asset ratio, and current ratio. Investment decisions represent the firm's policy in allocating funds to productive assets that support business growth and sustainability, and are measured through indicators including capital expenditure, total asset growth, and the investment opportunity set. Profitability functions as the mediating variable and describes the firm's ability to generate profits from the assets and capital utilized. This variable is measured using return on assets, return on equity, and net profit margin. The dependent variable in this study is firm value, which reflects market perceptions of the firm's performance and prospects. Firm value is measured using market-based indicators, including price to book value and Tobin's Q.

The data analysis technique employed in this study is multiple linear regression. In addition, mediation analysis is conducted to determine whether profitability acts as an intermediary variable in the relationship between financial management, investment decisions, and firm value. The mediation effect is tested using the Sobel test to evaluate the significance of the indirect influence of the independent variables on firm value through profitability. Through this analytical approach, the study aims to provide empirical evidence regarding the mechanism through which financial policies and investment decisions contribute to the creation of firm value.

RESULTS

Descriptive statistical analysis was conducted to provide an overview of the characteristics of research data, including financial management, investment decisions, profitability, and firm value in companies listed on the Indonesia Stock Exchange during the 2019–2023 period. The results of descriptive statistics show considerable variation between companies, reflecting differences in financial policy, investment intensity, as well as financial performance and market valuation.

Table 1. Descriptive Statistics of Research Variables

Variable	N	Minimum	Maximum	Mean	Standard Deviation
Financial Management (X ₁)	500	0.21	3.45	1.42	0.67
Investment Decision (X ₂)	500	-0.15	2.98	0.86	0.59
Profitability (M)	500	-0.12	0.41	0.09	0.08
Firm Value (Y)	500	0.38	6.72	1.89	1.21

Table 1 presents the descriptive statistics of the research variables, including financial management, investment decisions, profitability, and firm value, based on 500 observations. Financial management (X₁) has a minimum value of 0.21 and a maximum value of 3.45, with a mean of 1.42 and a standard deviation of 0.67, indicating a moderate level of financial structure management with a reasonable variation among firms. Investment decisions (X₂) show a minimum value of −0.15 and a maximum value of 2.98, with an average of 0.86 and a standard deviation of 0.59, suggesting that while some firms experienced a decline in investment or asset growth during certain periods, most firms still demonstrated positive investment activity. Profitability (M) ranges from −0.12 to 0.41, with a mean value of 0.09 and a standard deviation of 0.08, indicating that although some firms experienced losses in specific years, the overall sample firms were generally able to generate positive profits at a relatively modest level. Meanwhile, firm value (Y) has a minimum value of 0.38 and a maximum value of 6.72, with a mean of 1.89 and a standard deviation of 1.21, reflecting substantial variation in market valuation among firms, which may be influenced by differences in financial performance, growth prospects, and investor perceptions.

Table 2. Result of Financial Management and Investment Decision on Firm Value

Variable	Coefficient	t-statistic	p-value
Financial Management (X ₁)	0.083	1.21	0.227
Investment Decision (X ₂)	0.097	1.34	0.181
Constant	1.102	4.56	0.000
R ²	0.062		

Table 2 presents the regression results examining the effect of financial management and investment decisions on firm value. The results indicate that financial management ($\beta = 0.083$; $t = 1.21$; $p = 0.227$) and investment decisions ($\beta = 0.097$; $t = 1.34$; $p = 0.181$) do not have a statistically significant effect on firm value, as their significance levels exceed the 0.05 threshold. Although both variables show positive coefficients, their direct influence on firm value is not statistically supported. The constant value is 1.102 and is statistically significant ($t = 4.56$; $p = 0.000$). Furthermore, the coefficient of determination ($R^2 = 0.062$) indicates that financial management and investment decisions explain approximately 6.2% of the variation in firm value, while the remaining variation is explained by other variables outside the model.

Table 3. Results of Financial Management and Investment Decision on Profitability

Variable	Coefficient	t-statistic	p-value
Financial Management (X ₁)	0.214	3.98	0.000
Investment Decision (X ₂)	0.187	3.41	0.001
Constant	-0.021	-1.12	0.263
R ²	0.298		

Table 3 presents the regression results examining the effect of financial management and investment decisions on profitability. The results show that financial management ($\beta = 0.214$; $t = 3.98$; $p = 0.000$) has a positive and statistically significant effect on profitability. Similarly, investment decisions ($\beta = 0.187$; $t = 3.41$; $p = 0.001$) also demonstrate a positive and significant influence on profitability. These findings indicate that effective financial management and appropriate investment decisions contribute to improving a firm's profit performance. The constant value is -0.021 and is not statistically significant ($p = 0.263$). Furthermore, the coefficient of determination ($R^2 = 0.298$) suggests that financial management and investment decisions collectively explain approximately 29.8% of the variation in profitability, while the remaining variation is influenced by other factors not included in the model.

Table 4. Results of Profitability on Firm Value

Variable	Coefficient	t-statistic	p-value
Profitability (M)	0.463	6.87	0.000
Constant	0.912	3.94	0.000
R ²	0.341		

Table 4 presents the regression results examining the effect of profitability on firm value. The results indicate that profitability ($\beta = 0.463$; $t = 6.87$; $p = 0.000$) has a positive and statistically significant effect on firm value. This finding suggests that firms with higher profitability tend to have higher market valuation, as strong profit performance signals better financial prospects to investors. The constant value is 0.912 and is also statistically significant ($t = 3.94$; $p = 0.000$). Furthermore, the coefficient of determination ($R^2 = 0.341$) indicates that profitability explains approximately 34.1% of the variation in firm value, while the remaining variation is influenced by other variables outside the model.

Table 5. Mediation Results

Variable	Coefficient	t-statistic	p-value
Financial Management (X_1)	0.041	0.89	0.374
Investment Decision (X_2)	0.052	1.07	0.285
Profitability (M)	0.421	6.12	0.000
R ²	0.387		

Table 5 presents the mediation analysis results examining the roles of financial management, investment decisions, and profitability in influencing firm value. The results indicate that financial management ($\beta = 0.041$; $t = 0.89$; $p = 0.374$) and investment decisions ($\beta = 0.052$; $t = 1.07$; $p = 0.285$) do not have a statistically significant direct effect on firm value. In contrast, profitability ($\beta = 0.421$; $t = 6.12$; $p = 0.000$) shows a positive and significant effect on firm value. These findings suggest that profitability fully mediates the relationship between financial management, investment decisions, and firm value, indicating that these variables influence firm value only through profitability, rather than through their direct effects. Furthermore, the coefficient of determination ($R^2 = 0.387$) indicates that the model explains approximately 38.7% of the variation in firm value, while the remaining variation is influenced by other factors outside the model.

Table 6. Sobel Test Results

Mediation Path	Sobel Z	p-value
Financial Management $\rightarrow$ Profitability $\rightarrow$ Firm Value	3.94	0.000
Investment Decision $\rightarrow$ Profitability $\rightarrow$ Firm Value	3.21	0.001

Table 6 presents the results of the Sobel test used to examine the mediating role of profitability in the relationship between financial management, investment decisions, and firm value. The results show that the mediation path of profitability mediates the effect of financial management on firm value ($Z = 3.94$; $p = 0.000$), which is statistically significant, indicating that profitability significantly mediates the effect of financial

management on firm value. Similarly, the mediation path of profitability mediates the relationship between investment decisions and firm value ($Z = 3.21$; $p = 0.001$), which is also significant. These findings suggest that profitability functions as an important intermediary mechanism through which financial management and investment decisions influence firm value.

DISCUSSION

The findings of this study indicate that financial management does not have a significant direct effect on firm value, suggesting that the first hypothesis is not fully supported. This result implies that the management of funding structures, liquidity, and financial risk is not always immediately reflected in market valuation. In other words, investors may not automatically interpret financial policies as indicators of higher firm value unless these policies are accompanied by observable improvements in economic performance. This finding is consistent with previous studies, which reported that financial policies do not always directly increase firm value, particularly when the firm's debt structure generates additional financial risk (Pamungkas et al., 2021; Fu et al., 2022; Ebrahimi & Al-Najjar, 2025). These studies emphasize that excessive leverage or suboptimal funding structures may weaken investor confidence and limit the positive effect of financial management on firm value.

Similarly, the results show that investment decisions do not have a significant direct influence on firm value. Although investment activities such as capital expenditure and asset expansion are generally expected to enhance firm growth, the market does not always respond positively to these decisions. This finding supports prior empirical evidence suggesting that investment decisions do not necessarily increase firm value unless they are accompanied by clear improvements in operational outcomes and future cash flow prospects (Mahdi & Malik, 2024). Studies by Halik and Astuti et al. (2025) also indicate that inefficient or speculative investments may fail to attract positive market responses and may even increase uncertainty and financial risk from the perspective of investors. Therefore, investment decisions alone are not sufficient to enhance firm value without demonstrating tangible performance improvements.

In contrast, the results reveal that financial management has a positive and significant effect on profitability. This finding indicates that effective management of funding structures and liquidity contributes to improved cost efficiency and more optimal utilization of corporate resources. Firms that implement sound financial policies are better able to control operational costs and maximize the productivity of their assets, ultimately leading to stronger profit generation. This result is consistent with previous research showing that financial management practices are closely associated with higher profit performance and stronger internal financial stability (Kasbar et al., 2023).

The study also finds that investment decisions significantly influence profitability. Investments directed toward productive assets and strategic growth opportunities can enhance operational efficiency and increase a firm's capacity to generate profits. This finding is supported by prior studies, which demonstrate that asset expansion and capital expenditure contribute to higher profitability by strengthening production capacity and supporting long-term business growth (Girdzijauskas et al., 2022). However, these studies also emphasize that the effectiveness of investment decisions depends on the alignment between investment strategies and a firm's operational capabilities.

Furthermore, the results confirm that profitability has a positive and significant effect on firm value. Firms with stronger profit performance tend to receive higher market valuations because profitability signals financial strength, operational efficiency, and sustainable growth prospects. This finding is consistent with previous empirical studies, which show that profitability is one of the most important determinants of firm value, as it enhances investor confidence and improves expectations regarding future financial performance (Digdowiseiso et al., 2024; Arhinful et al., 2025).

The mediation analysis demonstrates that profitability significantly mediates the relationship between financial management, investment decisions, and firm value. This

finding indicates that financial policies and investment strategies influence firm value primarily through their impact on profit performance. Previous studies by Zhou et al. (2022) and Ghanad (2023) similarly argue that profitability functions as a transmission mechanism through which internal corporate policies are translated into market valuation outcomes. Therefore, the results reinforce the view that profitability plays a critical role in explaining how financial management and investment decisions ultimately contribute to the creation of firm value.

CONCLUSION

This study examines the relationships among financial management, investment decisions, profitability, and firm value in companies listed on the Indonesia Stock Exchange. The findings indicate that financial management and investment decisions do not have a significant direct effect on firm value. However, both variables significantly influence profitability, suggesting that effective financial policies and appropriate investment strategies contribute to improved profit performance. Furthermore, profitability is found to have a positive and significant effect on firm value and serves as a mediating variable in the relationship between financial management, investment decisions, and firm value. These results suggest that firm value is more strongly influenced by a firm's ability to generate sustainable profits rather than by financial and investment policies alone. Therefore, the practical implication of this study is that corporate management should prioritize financial and investment policies that are oriented toward enhancing profitability in order to strengthen investor confidence and increase firm value in the capital market.

Despite its contributions, this study has several limitations. The research focuses only on publicly listed companies and relies on secondary financial data within a specific observation period, which may not fully capture long-term financial dynamics or external factors affecting firm value. In addition, the research model explains only a portion of the variation in firm value, indicating that other important determinants may not have been included. Therefore, future research is recommended to incorporate additional variables such as corporate governance, business risk, macroeconomic conditions, and market competition. Expanding the sample scope and extending the observation period may also provide a more comprehensive understanding of the mechanisms influencing firm value across different industries and economic environments.

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