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The Role of Debt to Ratio and Profitability in Economic Growth and Company Development

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ABSTRACT

This study analyses the relationship and influence of Debt Asset Ratio (DAR) on company profitability. The data used in this study were obtained from the financial reports of companies listed on the Indonesia Stock Exchange during 2018-2022. The analytical method used is simple linear regression using statistical software. The steps are planning, collecting, analyzing, and interpreting data to answer research questions. DAR and profitability as variables in this study, population, and samples from 6 companies for five years. The influence of Debt to Asset Ratio applied to Company Profitability was analyzed using the linear regression statistical method. Debt to Asset Ratio is the independent variable, and Company Profitability is the dependent variable. The results of the correlation analysis found a linear relationship between the variables. The results of the regression analysis found that there was a shallow level of influence. This study has several limitations on the number of samples, variables, and industrial sectors studied. In addition, other factors also need to be considered-some recommendations for further research. They expanded the study sector, examining other factors such as accounts receivable turnover and company size.

Keywords: *debt to asset ratio, profitability, multiple linear regression, financial reports*

INTRODUCTION

The debt to asset ratio (DAR) is a metric used to assess how much a business relies on debt to finance its assets. DAR refers to the ratio of a company's assistance to its total debt. The ability of a corporation to make money from its operational activities is referred to as company profitability on the other hand. The debt level can have an impact on a company's performance and financial health, therefore understanding how it affects firm profitability is crucial.

The research analyzes the effect of Debt to Asset Ratio on company profitability. To understand the relationship between the level of corporate debt with financial performance and the resulting profit. By understanding this relationship, company management can make the right decisions in managing the capital structure and optimizing profitability.

Debt to Asset Ratio

The ratio known as the debt to asset ratio (DTAR) is used to calculate how much a business borrows to finance its assets. The percentage of a company's total assets that are financed by debt is indicated by this ratio. DTAR is calculated by dividing a company's total debt by its total assets, multiplying the result by 100 to obtain a percentage. The DTAR ratio illustrates the level of dependence of the company on UT. The higher this ratio, the greater the proportion of assets debt financing might raise the financial risk for the business. Conversely, if the DTAR ratio is low, the company has more assets financed by its capital than debt. The Debt to Asset Ratio is a comparison When calculating how much of the company's assets are financed by total debt, net capital, which is the difference between the value of debt and the value of assets, is used (Kasmir, 2019; Sutrisno, E. 2017; Damaianti, V. S., & Syamsuddin, A. R. 2006).

Company Profitability

The ability of a corporation to make a profit from its operations is referred to as profitability. Financial performance indicators including Return on Assets (ROA), Return on Equity (ROE), and Gross Profit Margin are measured by a number of metrics. ROA gauges how effectively a business uses its resources to produce profits. The ROE calculates the rate of return to shareholders by comparing the company's net income with shareholder equity. Gross Profit Margin describes the percentage of a company's gross profit from sales revenue. High profitability shows that the company can generate good profits from its operations. This can reflect operational efficiency, competitive advantage, and sound financial management. The profitability ratio measures and assesses a company's ability to seek profits from sales, total assets, and own capital during a certain period (Kasmir, 2018; Agus Sartono, 2008; Bambang Riyanto, 2008).

Relationship between Debt to Asset Ratio and Company Profitability

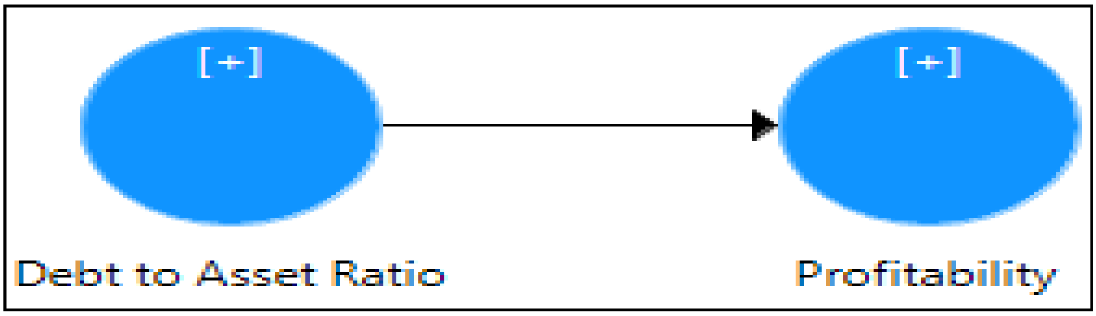
The relationship between DTAR and a company's profitability can vary depending on various factors, including the industry, business cycles, and financial strategy. In general, a high DTAR ratio can hurt a company's profitability. This is caused by the interest expense that the company must pay on its debt. The higher the DTAR ratio, the greater the interest expense that must be borne by the company, which can reduce the generated net profit.

However, the relationship between DTAR and profitability is dynamic. In some cases, using debt in asset financing can increase company profitability. For example, if a company uses low-cost debt to finance high-profit investments, a high DTAR ratio may not significantly affect the company's profitability.

The study's findings demonstrate that the debt to asset ratio (DAR) is not harmful and that partial returns on assets do not significantly affect firm value. Debt to Asset Ratio has a negative but small impact on Return on Equity and a negative but insignificant impact on profitability ratios (Amelia, L., & Wijay, H. 2023; Arrahman, A., Murni, S., & Mangantar, M. 2023; Nugroho, D., Riyanti, & Hakim, L. 2023). In addition, the results of other studies show that profitability is impacted by the ratio of debt to assets. The debt to equity ratio (DER) has a positive (unidirectional) impact on mining companies' return on assets (Apriliana, M., Wafirotin, K. Z., & Wijayanti, I. 2023; Jannah, M., Tarmizi, & Habibah, G. W. . A. 2021).

It is important to note that an analysis of the relationship between DTAR and company profitability should be carried out, taking into account the context and unique characteristics of the company. In addition, other factors such as market risk, capital structure, and economic conditions also need to be considered in evaluating the relationship between DTAR and company profitability.

Figure 1. Concept Framework



RESEARCH METHODS

The population and sample data used in the study were taken from data from 7 LQ45 businesses that will be on the IDX from 2018 to 2022. The data collection technique used to collect the information needed in the research is document studies and company financial report data from the IDX. The data analysis process uses Smart PLS software with an inner model test to answer research questions and test the hypotheses proposed.

RESULTS AND DISCUSSION

Results

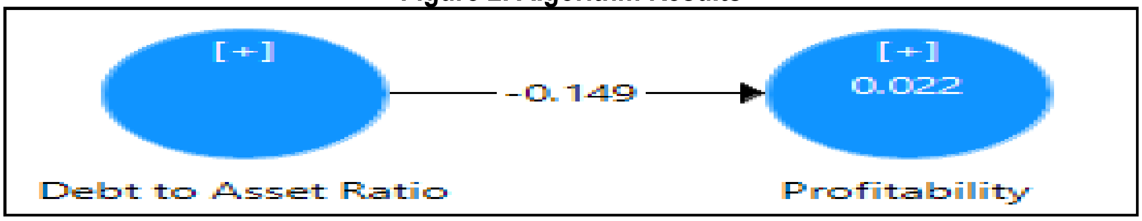
Table 1 shows the findings of the descriptive analysis test for this study, including the minimum, maximum, and average scores.

Table 1. Descriptive Statistics

	N	Minimum	Maximum	Mean
Debt to Asset Ratio (%)	35	12.749	33.068	20.00000
Profitability (%)	35	-2.868	62.974	20.00000

Table 1's results show that the minimum and maximum of DAR (12,749 and 33,068), Profitability (-2,868 and 62,974), with the same average score in (%).

Figure 2. Algorithm Results



The results of the algorithm test in Figure 2 show that the path coefficients (-0.149) have a negative slope. The same thing can also be seen in the following beam diagram in Figure 3.

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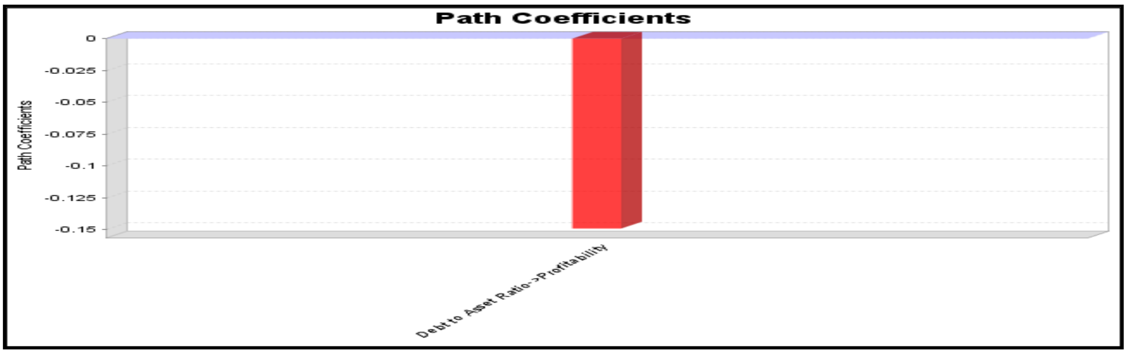
Figure 3. Path Coefficients



Next, to make it easier to observe the path coefficients test results, the test results are also displayed in tabular form, as seen in Table 2 below.

Table 2. Path Coefficients

Variables	Coefficients	Explanation
Debt to Asset Ratio → Profitability	-0.149	Negatives

The results in Table 2 also offer the same path coefficients (-0.149). Furthermore, the results of the Additionally, R Square The accompanying figure and table display adjusted tests. Can be seen in Figures 4, 5, and Table 3 are included.

Figure 4. R Square

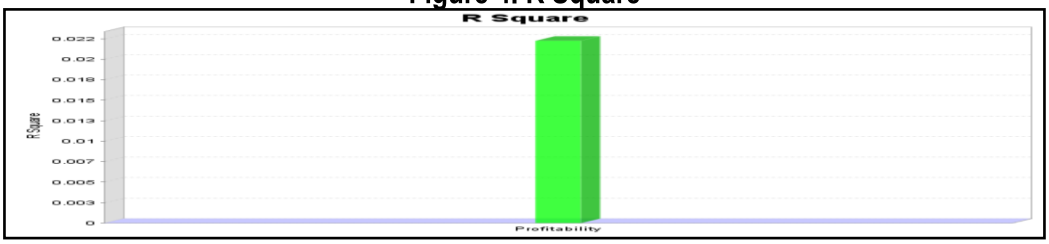


Figure 5. R Square Adjusted

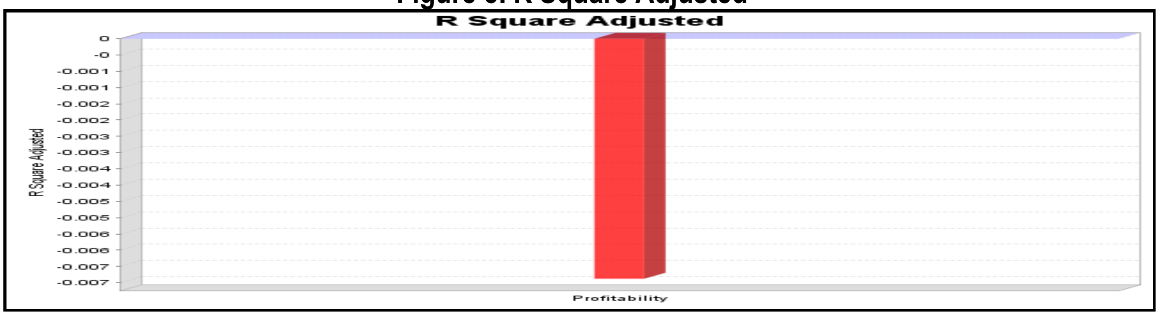


Table 3. R Square, R Square Adjusted

Variables	R Square	R Square Adjusted
Profitability	0.022	-0.007

The results in the figure and table above explain the R Square value of (0.022) and Adjusted RSquare (-0.007). Figures 6 and 7 and Table 4 show the results of the bootstrapping test to test the proposed hypothesis.

Figure 6. Bootstrapping

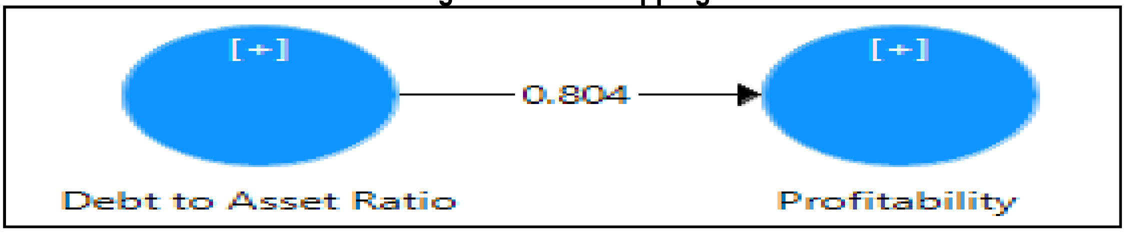


Figure 7. Debt to Asset Ratio and Profitability

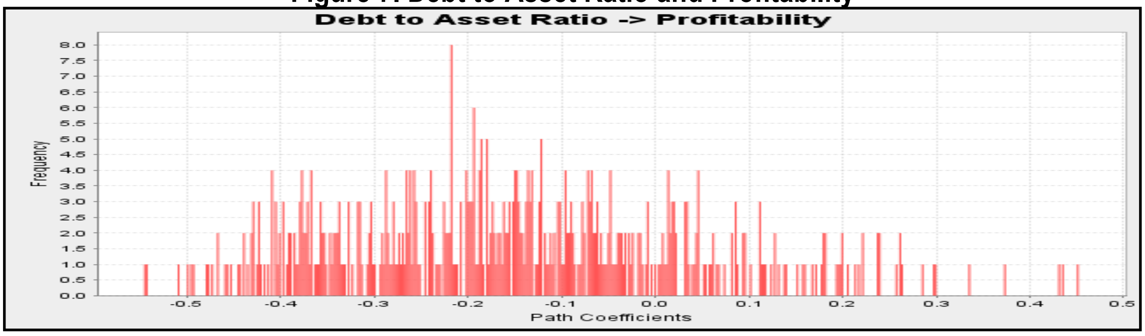


Table 4. Path Coefficients, T-Values, P-Values

Variables	T Statistics	P Values	Description
Debt to Asset Ratio -> Profitability	0.804	**0.422**	**Not Significant**

The results of Lottery 4 show the T Statistics value (0.804) and P Value (0.422). This indicates that the DAR on profitability has an insignificant relationship and influence.

CONCLUSION

A financial indicator called the debt-to-asset ratio quantifies the percentage of a company's total assets that are financed by debt. It shows the degree of financial risk or leverage a company has taken on. The industry, the state of the economy, and the particulars of the company can all have an impact on how the debt-to-asset ratio affects a company's profitability.
A higher debt-to-asset ratio generally means that a larger portion of a company's assets is financed by debt. This can have positive and negative effects on profitability:

1. Positive Effects:

- ➔ Tax advantage: Companies that use debt financing are able to deduct interest costs from their taxable income, which lowers their overall tax liability and could lead to higher profits.
- ➔ Leverage amplification: If a company can earn a higher return on its assets than the cost of borrowing, taking on debt can magnify shareholder returns and boost profitability.
- ➔ Increased investment potential: Debt financing provides additional funds that can be used for growth initiatives, such as expanding operations, investing in new projects, or acquiring assets. If these investments generate higher returns, they can positively impact profitability.

2. Negative Effects:

- ➔ Interest expense: Higher debt levels increase interest payments, affecting a company's profits. If the interest expense surpasses the returns generated by the assets, it can lead to reduced profitability.
- ➔ Financial risk: High A corporation may be more susceptible to economic downturns or changes in interest rates if it has higher debt levels. This added risk can negatively impact profitability, especially if the company struggles to meet its debt obligations.
- ➔ Restricted financial flexibility: Excessive debt can limit The capacity of a business to adapt to shifting market circumstances or seize new possibilities. A lack of flexibility can hinder profitability in a dynamic business environment.

Ultimately, the optimal debt-to-asset ratio depends on factors such as industry norms, management's risk tolerance, and the company's specific circumstances. Companies must balance debt and profitability, considering the potential benefits of leverage while mitigating the associated risks.

The path coefficients test findings reveal a negative association and a small effect. The results of this investigation are consistent with the findings of (Amelia, L., & Wijay, H. 2023; Arrahman, A., Murni, S., & Mangantar, M. 2023; Nugroho, D., Riyanti, & Hakim, L. 2023)

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