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Minimizing Manufacturing Industry Capital Costs through Governance, Corporate Risk Management, Social Responsibility and Company Size

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Abstract

This research aims to analyze the influence of corporate governance, corporate risk management, corporate social responsibility, and company size on the cost of capital in the manufacturing industry listed on the Indonesia Stock Exchange. This research design is quantitative, with samples taken using non-random techniques, such as purposive sampling or judgment sampling, so that the total research sample is 45 companies, with a research period of 4 years and a total of 180 research data. The data analysis technique uses panel data with path analysis. The research results show that implementing broad and integrated corporate risk management reduces the cost of capital. Large company size can increase the cost of capital in manufacturing industrial companies listed on the Indonesian Stock Exchange. Meanwhile, the implementation of corporate governance and corporate social responsibility does not reduce the company's capital cost. Future advice is that company management is expected to pay more attention to management practices related to corporate social responsibility, corporate risk management, and capital costs because these factors impact increasing the value and survival of the company in the future. Management also needs to pay attention to the role of capital costs, which can mediate the implementation of corporate risk management in increasing company value.

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1. Introduction

Company value is an integral part of the company because it can reflect its overall performance and influence investors' views of the company. Company value is the market value of the company's debt and equity securities in circulation (Keown et al., 2014). Company value is investors' perception of the company's level of success, which is often linked to share prices (Syofyan et al., 2020). A high share price reflects the company's high value. A high company value will make the market believe not only in the company's current performance but also in the company's prospects (Gunadi et al., 2020).

Company value is an exciting topic to continue to study because company value can be a measure of how much bargaining power a company has in the eyes of investors (Maher & Aquanno, 2020). The higher the company value, the higher the welfare of investors will be. For company value to increase, there must be synergy between shareholders and related stakeholders in determining the right decisions (Battilana et al., 2020). Stock price fluctuations are a phenomenon related to company value. Company value is investors' perception of the company's level of success, which is generally linked to share prices. The results of measuring company value are greatly influenced by the market value of equity or market capitalization value, which is obtained by multiplying the share price and the number of shares outstanding. Conflicts between shareholders and managers often occur when companies try to increase company value, which often leads to company failure. Corporate needs arise from potential conflicts of interest between managers and shareholders due to the separation of ownership and management functions. Shareholders are interested in maximizing firm value, while managers' goals may also include increasing personal wealth, job security, and prestige.

Corporate governance is a crucial problem currently being faced. Good corporate governance is one of the principles for managing a company well so that in the future, the company can maximize the profits of its owners. However, in its development, the condition of corporate governance practices in Indonesia generally has yet to achieve good results. The results of the ACGA (Asian et al. Association) survey show that the ranking for the implementation of corporate governance in Indonesia is not encouraging (Wahyudi, 2021). This condition is indicated by the increasing number of corporate governance violations that do not receive warnings from regulators.

This research was conducted on manufacturing industry sector companies listed on the Indonesia Stock Exchangekn. The manufacturing industry is the industry that has the most significant number of issuers on the Indonesian Stock Exchange. Manufacturing industrial companies are often considered companies with strategic value in investors' eyes because they have a high return on investment.

The manufacturing industry is a sector that many investors are interested in investing in because it has the second highest market capitalization value after the financial industry (Nikonenko et al., 2020). The manufacturing industry plays a vital role as an engine of development because the manufacturing industry has several advantages compared to other sectors, seen from its huge embedded capital capacity, the ability to absorb a large local workforce, and the ability to create added value from every input in the production process.

This research aims to analyze the influence of corporate governance, corporate risk management, corporate social responsibility, and company size on the cost of capital in the manufacturing industry listed on the Indonesia Stock Exchange. The theoretical benefit of this research is that it can enrich scientific conceptions, especially regarding the mediating role of the cost of capital in the relationship between corporate governance, corporate risk management, corporate social responsibility, and company size. It is hoped that the practical benefits of this research for companies will contribute to thinking about the importance of good corporate governance, the implementation of corporate risk management, reported corporate social responsibility activities, and the cost of capital as a basis for consideration in making company policies to increase company value. For investors, it provides information in considering aspects that need to be taken into account in investing, apart from considering monetary measures but also paying attention to aspects of corporate governance, corporate risk management, disclosure of corporate social responsibility, and company size.

Literature Review

Stakeholder theory states that a company is not only an entity that operates for its interests but must also benefit its stakeholders, including shareholders, creditors, suppliers, government, society, and other interested parties. Ghozali and Chariri (2007) said that the support given by stakeholders to the company is very influential in the company's sustainability.

Jensen and Meckling (1976) stated that a phenomenon that often occurs in agency contracts is that agents do not act in the interests of shareholders. Agency theory is closely tied to conflicts between shareholders and managers. This conflict occurs because of differences in interests between the agent and the principal and is supported by information asymmetry.

Agency theory is the basis for the birth of corporate governance, where companies are expected to be well-managed and controlled so that no party is harmed by information asymmetry in agency conflicts. Corporate governance is a system that regulates and controls companies that can provide and increase company value to shareholders (Brown & Caylor, 2006). Good organizational governance relates to how the organization organizes its structure effectively and how the policy-making process is carried out correctly and fairly. It refers to the principles of good corporate governance, namely transparency, accountability, responsibility, independence and fairness.

According to the Committee of Sponsoring Organizations of the Treadway Commission (COSO, 2004), corporate risk management is a process influenced by management, the board of directors, and other personnel that is carried out in determining strategy and covers the organization as a whole, designed to identify events that cause has the potential to influence the organization, and manage risks, as well as provide adequate confidence regarding the achievement of organizational goals.

Company size is the company's size, which is indicated or can be measured by total assets, total sales, total profits, and tax burden (Nurwati et al., 2021). Company size is a proxy for financial strength as a scale for classifying whether a company is large or small. One benchmark for indicating the size of a company uses total company assets (Dang et al., 2019; Hirdinis, 2019; Niresh & Velnampy, 2014). Thus, it is a hypothesis. This research is: H1a) Corporate governance has a significant adverse effect on the cost of capital. H1b) Corporate risk management significantly negatively affects the cost of capital. H1c) Corporate social responsibility significantly negatively affects the cost of capital. H1d) Company size has a negative and significant effect on the cost of capital.

2. Methods

This research is quantitative. This research plan or design uses a causality research design, namely a research design used to test the influence, relationship or impact of independent variables on the dependent variable (Chandrarin, 2017). The population of this research is all companies in the manufacturing industry sector listed on the Indonesia Stock Exchange in the 2016-2019 period. This research sample was taken using a non-random technique, purposive sampling or judgment sampling. Based on the sample selection procedure in Table 5 above, the total research sample was 45 companies, with a research period of 4 years, so the total research data was 180. This quantitative study analyzes the influence of corporate governance, corporate risk management, corporate social responsibility, and company size on company value through the cost of capital variable in the manufacturing industry listed on the Indonesia Stock Exchange. The data analysis technique in this research uses panel data analysis. Panel data is a combination of time series data and cross-section data. Hypothesis testing is carried out using a panel data regression model.

3. Results and Discussion

3.1. Results

The results of data analysis regarding the direct influence of corporate governance, corporate risk management, corporate social responsibility, and company size on the cost of capital can be explained as follows:

Table 1. Research Variable Path Coefficient

Variable	Direct Influence	p-value	Information
Corporate Governance -> Capital Cost	-0.066053	0.1147	Not Sig.
Corporate Risk Management -> Capital Costs	-0.177625	0.0043*	Sig.
Corporate Social Responsibility -> Capital costs	0.604761	0.0782	Not Sig.
Company Size -> Capital costs	0.363112	0.0000*	Sig.

Source: Data Processed (2024)

a. Corporate governance does not hurt the cost of capital. This is indicated by the path coefficient value of -0.066053, which is not statistically significant because the α value 0.1147 is greater than 0.05.
b. Company risk management hurts the cost of capital. This is indicated by the path coefficient value of -0.177625, which is statistically significant because the α value of 0.0043 is smaller than 0.05.

c. Corporate social responsibility does not hurt the cost of capital. This is indicated by the path coefficient value of 0.604761, which is not statistically significant because the α value of 0.0782 is greater than 0.05.
d. Company size has a positive effect on the cost of capital. This is indicated by the path coefficient value of 0.363112, which is statistically significant where the α value of 0.000 is smaller than 0.05.

The statistical test results of hypothesis 1a show that corporate governance does not hurt the cost of capital. The research results show that the regression coefficient of corporate governance on the cost of capital is -0.066053 with a significance value of 0.1147, more significant than 0.05. This means that corporate governance does not negatively and significantly affect the cost of capital.

The statistical test results of hypothesis 1b show that corporate risk management negatively and significantly affects the cost of capital. The research results show that the regression coefficient for corporate risk management on the cost of capital is -0.177625 with a significance value of 0.0043, which is smaller than 0.05. This means that corporate risk management has a negative and significant effect on the tested cost of capital. The better corporate risk management, the lower the company's cost of capital.

The statistical test results of hypothesis 1c show that corporate social responsibility does not hurt the cost of capital. The research results show that the regression coefficient of corporate social responsibility on the cost of capital is 0.604761, with a significance value of 0.0782, more significant than 0.05. This means that corporate social responsibility does not negatively and significantly affect the cost of capital.

The statistical test results for hypothesis 1d show that company size has a positive and significant effect on the cost of capital. The research results show that the regression coefficient of company size on the cost of capital is positive at 0.363112 with a significance value of 0.000, which is smaller than 0.05. This means that company size has a positive and significant effect on the cost of capital, so hypothesis 1d, which states that company size hurts the cost of capital, is not tested.

3.2. Discussion

The research results reveal that corporate governance does not impact the cost of capital. The cost of capital relates to the minimum rate of return required by investors. The company's governance, which includes an independent board of commissioners, members of the board of commissioners, an audit committee, and the number of management shares in this research, cannot reduce the cost of capital due to several factors. First, managerial share ownership, which is the percentage of shares owned by management, is still low; some sample companies do not even have managerial shares, so this cannot reduce the misalignment of incentives and interests between management and outside shareholders, which is a cost to the company. So that it does not impact the return required by shareholders and reduces the cost of capital. Supposedly, managerial ownership can reduce conflict between the owner (agent) and management. Agency conflicts can potentially increase agency costs and risk, ultimately increasing the cost of capital, especially the cost of own capital. Second, creditors and shareholders ignore the company's governance factors. The number of members of the Board of Commissioners and the number of members of the independent Board of Commissioners is seen as a necessity in the company to meet regulatory requirements so that it is separate from the return required by investors.

The research results are different from those of several previous studies, which revealed that good corporate governance is a mechanism that can guarantee a company's creditors and shareholders a return on their investment (Fermania, 2014; Shleifer & Vishny, 1997). The results of this research are in line with research by Dogan and Acar (2020), which revealed that corporate governance, as measured by institutional ownership, does not affect the cost of capital. Conflicts of interest and attitudes that conflict with the company's interests can hurt shareholders and the cost of capital. An increase in the number of company board members increases the capital costs incurred by the company (Dogan and Acar, 2020).

Companies that can identify, measure, and manage risks at levels determined by the company will be able to minimize the costs of using capital borne by the company. The research results reveal that corporate risk management will reduce the cost of capital because the company can mitigate the risks faced so that the potential risk is reduced, ultimately reducing the return required by shareholders and reducing the cost of capital itself. The cost of foreign capital can also be reduced because creditors have confidence in the security of funds lent to the company. This shows that well-managed corporate risk management, where the company has excellent risk mitigation capabilities, can reduce the capital costs incurred. The research supports previous research that examines the relationship between corporate risk management and the cost of capital, such as Berry-Stölzle & Xu (2018) and McShane et al. (2011).

According to Berry-Stölzle & Xu (2018), corporate risk management increases information about a company's risk profile. Therefore, adopting corporate risk management can reduce a company's cost of capital. According to McShane et al. (2011), implementing corporate risk management can influence a company's capital structure, which means how it finances investments with equity and debt to achieve its goals. Raising debt and equity capital incurs costs such as interest payments and other financial obligations. According to COSO (2004), corporate risk management helps reduce a company's total risk by reducing earnings volatility and increasing capital use effectiveness (McShane et al., 2011). A well-implemented corporate risk management program reduces risk and motivates debt markets to provide lower-cost financing (Berry-Stölzle & Xu, 2018).

Research strengthens the argument that risk management can reduce a company's cost of capital. To date, the predominant view in the risk management literature is that risk management creates value through its impact on a company's cash flows. Risk management can reduce corporate tax liabilities, bankruptcy transaction costs, and regulatory costs, as well as reduce the problem of underinvestment in financially constrained companies, leading to higher profits (Berry-Stölzle & Xu, 2018). Corporate risk management impacts cash flow and company income and can reduce the company's cost of capital (Hoyt & Liebenberg, 2011).

Disclosure of corporate social responsibility cannot reduce the company's cost of capital. This is illustrated by the research results that most corporate social responsibility disclosures are still low. The value of corporate responsibility disclosure has no impact on changes in the company's cost of capital, both the cost of own capital and the cost of debt capital. A low score for corporate social responsibility does not reduce the cost of capital. Investors and creditors in the market ignore corporate social responsibility performance when investing their funds or channeling credit within the company.

Disclosure of corporate social responsibility in this study does not contribute to the cost of capital. Disclosure of economic performance items which are reflected in the economic value generated and distributed directly, including income, operator costs, compensation to employees, donations and investments to the community, retained earnings, and payments to capital providers and governments, which are always disclosed by the company as well as environmental category disclosures which are reflected in the percentage of products sold and their packaging that are reclaimed by category does not play a role in the company's decision making in making capital investments. When making investments, companies do not consider disclosure of corporate social responsibility, so disclosure of corporate social responsibility is not directly related to the level of return required by investors and the risks of the investment, so it does not have an impact on reducing the cost of capital. The research results are supported by research by Piechocka-Kałużna et al (2021), which cannot prove the role of social responsibility in changes in a company's cost of capital.

Company size, as measured by total assets, plays a role in increasing the cost of capital. The more significant the company size, the higher the capital costs incurred. The research results show that companies that operate with significant assets have a high risk of managing their assets and tend to have significant capital costs.

The research results reveal that company size is reflected in the total assets owned by the company, both current assets, fixed assets and other assets. Significant total assets indicate large investments, where funding comes from one's own capital and foreign capital. Significant investments require enormous capital costs. A company size that is too large is one of the causes of inefficiency in monitoring operational and strategic activities by management, which can reduce company value. In addition, the company's large size, which is reflected in total assets, reflects the large amount of company funds that are absorbed to meet short-term debt financing and fixed asset expenditure that is not directly related to the company's operations. This will increase the cost of capital.

Based on sample company data, companies with significant assets have a capital structure with more outstanding capital than foreign capital. Large companies will find it easier to obtain capital in the capital market than smaller companies. Capital obtained in the capital market has a higher cost of capital compared to the cost of debt because, from the investor's perspective, investors have a higher risk if they invest their funds in the form of shares or their own capital because there is no guarantee for the funds invested. Therefore, investors require a higher return than debt. Apart from that, the cost of issuing ordinary shares will also increase the cost of capital itself. For this reason, large companies tend to have high capital costs themselves.

If the company chooses to fund the company through increasing debt, according to the Trade-off theory (Brigham & Houston, 1996), more debt results in increasing the risk borne by shareholders (equity) and also increasing the expected rate of return and will increase the cost of capital, especially cost of loan capital.

4. Conclusion

Based on the results of research and discussion regarding the influence of corporate governance, corporate risk management, corporate social responsibility, company size, and cost of capital, it can be concluded that corporate governance results from analysis of control factors consisting of the number of independent commissioners, the number of board of commissioners, the number of audit committees. , and percentage of management shares. Factors in corporate governance describe the implementation of the principles of openness, accountability, independence, equality and fairness in the company. The implementation of corporate risk management shows that the average corporate risk management is at an adequate level, where the company has a risk control system for the principal risks it faces. The company can identify risks well and carry out a risk intimidation process to minimize the risks that occur. Corporate social responsibility shows that the value of corporate social responsibility disclosure is still low. The implementation of broad and integrated corporate risk management has an impact on reducing the cost of capital. Large company size can increase the capital costs of manufacturing industrial companies listed on the Indonesian Stock Exchange. Meanwhile, the implementation of corporate governance and the implementation of corporate social responsibility do not play a role in reducing the company's cost of capital.

Based on the research results and discussion above, several suggestions need to be made for company management in this research. They should pay more attention to management practices related to corporate social responsibility, corporate risk management, and the cost of capital because these factors will increase the value and survival of the company in the future. Management also needs to pay attention to the role of capital costs, which can mediate the implementation of corporate risk management in increasing company value. For future researchers, this research can be a basis for conducting further research related to corporate governance. The research used indicators of corporate governance attributes from the control side, including the number of independent commissioners, members of the board of commissioners, audit committees, and percentage of management shares. Researchers found no governance influence on the cost of capital or company value. Future research can use other indicators, such as the corporate governance index, to see the relationship between corporate governance and the cost of capital and firm value.

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