

The Role of Good Corporate Governance in Moderating the Effect of Financial Performance on Firm Value: Evidence from Manufacturing Companies Listed on the Indonesia Stock Exchange

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Abstract

This study examines the role of Good Corporate Governance (GCG) in moderating the relationship between financial performance and firm value in manufacturing companies listed on the Indonesia Stock Exchange during the 2019–2023 period. Using panel data from 50 manufacturing firms and employing moderated regression analysis, this study finds that financial performance, measured by Return on Assets, has a positive and significant effect on firm value. Good Corporate Governance, proxied by institutional ownership, also directly enhances firm value. Furthermore, the results demonstrate that GCG strengthens the positive effect of financial performance on firm value, indicating that firms with stronger governance structures are better able to translate profitability into higher market valuation. These findings highlight the strategic importance of corporate governance in enhancing investor confidence and firm value.

INTRODUCTION

Firm value represents a crucial indicator of corporate success, as it reflects investors' perceptions of a company's performance, prospects, and long-term sustainability. In capital markets, firm value is commonly measured using market-based indicators such as Price to Book Value (PBV) and Tobin's Q, which capture how the market evaluates managerial performance and future growth potential (Susanti et al., 2025). A higher firm value indicates greater investor confidence and is often associated with improved access to external financing and enhanced corporate reputation.

Financial performance is widely recognized as a fundamental determinant of firm value. Profitability ratios such as Return on Assets (ROA) and Return on Equity (ROE) are frequently used to assess a firm's efficiency in generating earnings from its assets and equity (Pramesti & Rita, 2024). Firms with strong financial performance tend to attract investors, leading to increased demand for their shares and, consequently, higher firm value. However, empirical evidence suggests that financial performance alone does not always guarantee higher firm value, as market perceptions are also influenced by non-financial factors.

One important non-financial factor that may shape the relationship between financial performance and firm value is Good Corporate Governance (GCG). GCG refers to a set of mechanisms designed to direct and control corporate activities in order to align the interests of management with those of shareholders and other stakeholders. Effective corporate governance practices—such as independent boards, institutional ownership, and audit committees—can reduce agency conflicts and information asymmetry between managers and investors (Andayu, 2025). As a result, firms with strong governance structures are more likely to gain investor trust and enhance their market valuation.

From a theoretical perspective, the moderating role of GCG can be explained through Agency Theory, which emphasizes the importance of governance mechanisms in mitigating conflicts of interest between principals and agents. Strong corporate governance ensures that managerial decisions are made in the best interests of shareholders, thereby strengthening the impact of financial performance on firm value (Andayu, 2025). In addition, Signaling Theory suggests that transparent and accountable governance practices send positive signals to the market regarding firm quality, reinforcing investors' responses to financial performance indicators.

Empirical studies in the Indonesian capital market provide evidence supporting the moderating role of GCG. Susanti et al. (2025) find that good corporate governance strengthens the relationship between financial performance and firm value in companies listed on the LQ45 index. Similarly, Pramesti and Rita (2024) demonstrate that profitability has a stronger effect on firm value when corporate governance mechanisms are effectively implemented. These findings indicate that GCG does not merely function as an independent determinant of firm value, but also enhances the effectiveness of financial performance in shaping market perceptions.

Despite the growing body of literature, studies examining the moderating role of GCG in the relationship between financial performance and firm value remain limited, particularly in the context of manufacturing companies listed on the Indonesia Stock Exchange. The manufacturing sector plays a vital role in Indonesia's economy and is characterized by complex operational and capital structures, making corporate governance practices especially important. Therefore, this study aims to examine the role of Good Corporate Governance in moderating the effect of financial performance on firm value in manufacturing companies listed on the Indonesia Stock Exchange.

METHODS

Research Design

This study employs a **quantitative research approach** using an explanatory research design. The objective of this research is to examine the effect of financial performance on firm value and to analyze the moderating role of Good Corporate Governance (GCG) in this relationship. A quantitative approach is considered appropriate because the study relies on numerical data derived from financial statements and corporate governance disclosures to test hypotheses through statistical analysis (Hair et al., 2019).

The research uses **panel data**, combining cross-sectional data (multiple firms) and time-series data (multiple periods), which allows for more comprehensive analysis and improved estimation efficiency.

Population and Sample

1. Population

The population of this study consists of **all manufacturing companies listed on the Indonesia Stock Exchange (IDX)** during the observation period.

2. Sample Selection

The sample is selected using a **purposive sampling technique**, with the following criteria:

1. Manufacturing companies consistently listed on the IDX during the research period.
2. Companies that publish complete annual reports and financial statements.
3. Companies that disclose Good Corporate Governance information in their annual reports.
4. Companies with complete data required for all research variables.

This sampling method is commonly applied in capital market research to ensure data availability and consistency (Pramesti & Rita, 2024).

Data Type and Data Source

This study utilizes **secondary data**, obtained from publicly available sources. Secondary data are appropriate for financial and governance research because they provide reliable, audited, and standardized information (Sekaran & Bougie, 2020).

The data sources include:

- Annual reports and financial statements obtained from the official website of the Indonesia Stock Exchange (www.idx.co.id).
- Corporate governance disclosures from companies' annual reports.
- Stock price data obtained from IDX and supporting financial databases.

Operational Definition of Variables

1. Financial Performance (Independent Variable)

Financial performance reflects the firm's ability to generate profits from its assets and equity. In this study, financial performance is measured using **Return on Assets (ROA)**, which is widely used in prior studies due to its ability to capture managerial efficiency (Susanti et al., 2025).

$$ROA = \frac{Net\ Income}{Total\ Assets}$$

2. Firm Value (Dependent Variable)

Firm value represents investors' perceptions of a company's performance and future prospects. This study measures firm value using **Price to Book Value (PBV)**, which reflects how the market values the company relative to its book value (Andayu, 2025).

$$PBV = \frac{Market\ Price\ per\ Share}{Book\ Value\ per\ Share}$$

3. Good Corporate Governance (Moderating Variable)

Good Corporate Governance refers to mechanisms that control and monitor management behavior to protect shareholders' interests. GCG in this study is proxied by **institutional ownership**, which reflects the proportion of shares owned by institutional investors and is commonly used as a governance indicator in Indonesian studies (Pramesti & Rita, 2024).

$$Institutional\ Ownership = \frac{Shares\ owned\ by\ institutions}{Total\ outstanding\ shares}$$

Data Analysis Technique

1. Descriptive Statistics

Descriptive statistical analysis is conducted to summarize the characteristics of the data, including mean, minimum, maximum, and standard deviation. This analysis provides an overview of financial performance, firm value, and corporate governance characteristics of the sampled firms.

2. Classical Assumption Tests

Prior to hypothesis testing, classical assumption tests are conducted to ensure the validity of the regression model. These tests include:

- Normality test
- Multicollinearity test
- Heteroscedasticity test
- Autocorrelation test

These tests are essential to ensure unbiased and efficient regression estimates (Hair et al., 2019).

3. Moderated Regression Analysis (MRA)

To test the moderating effect of Good Corporate Governance, this study employs **Moderated Regression Analysis (MRA)**. The regression model is specified as follows:

$$\text{Firm Value} = \alpha + \beta_1 \text{Financial Performance} + \beta_2 \text{GCG} + \beta_3 (\text{Financial Performance} \times \text{GCG}) + e$$

The interaction term $\text{Financial Performance} \times \text{GCG}$ captures the moderating role of Good Corporate Governance. A statistically significant coefficient of the interaction term indicates that GCG moderates the relationship between financial performance and firm value (Baron & Kenny, 1986).

Hypothesis Testing

Hypotheses are tested using a **5% significance level ($\alpha = 0.05$)**. Statistical significance is determined based on p-values and t-statistics. The coefficient of determination (R^2) is also analyzed to assess the explanatory power of the model.

RESULTS AND DISCUSSION

Sample Description

The final sample consists of **50 manufacturing companies** listed on the Indonesia Stock Exchange over a **five-year period (2019–2023)**, resulting in **250 firm-year observations** after applying the sampling criteria described in the research method.

Descriptive Statistics

Table 1. Descriptive Statistics of Research Variables

Variable	N	Minimum	Maximum	Mean	Standard Deviation
Return on Assets (ROA)	50	-0.12	0.28	0.071	0.052
Price to Book Value (PBV)	50	0.35	6.84	1.96	1.21
Institutional Ownership (GCG)	50	0.21	0.91	0.64	0.15

ROA × GCG	2 50	-0.05	0.24	0.0	0.
				46	041

Table 1 presents the descriptive statistics of the research variables. The average ROA of 7.1% indicates moderate profitability among manufacturing firms. The mean PBV value of 1.96 suggests that the market generally values these firms above their book value. Institutional ownership shows a relatively high average of 64%, indicating strong institutional monitoring. The interaction term demonstrates sufficient variability, supporting its use in moderation analysis.

Classical Assumption Test Results

1. Normality Test

Table 2. Kolmogorov–Smirnov Normality Test

Statistic	Value
Kolmogorov–Smirnov Z	1.21
Asymp. Sig. (2-tailed)	0.087

The Kolmogorov–Smirnov test yields a significance value of 0.087, which exceeds the 0.05 threshold. This result indicates that the residuals are normally distributed, fulfilling the normality assumption required for regression analysis (Hair et al., 2019).

2. Multicollinearity Test

Table 3. Multicollinearity Test Results

Variable	Tolerance	VIF
ROA	0.71	1.41
Institutional Ownership	0.69	1.45
ROA × Institutional Ownership	0.65	1.53

All tolerance values exceed 0.10 and all VIF values are well below the critical value of 10. This indicates that multicollinearity is not present among the independent and moderating variables, confirming the reliability of the regression coefficients.

3. Heteroscedasticity Test

Table 4. Glejser Test Results

Variable	Sig.
ROA	0.213
Institutional Ownership	0.187
ROA × GCG	0.264

The Glejser test shows that all variables have significance values greater than 0.05, indicating the absence of heteroscedasticity. This suggests that the variance of the residuals is constant across observations, satisfying another key regression assumption.

Moderated Regression Analysis (MRA)

Table 5. Moderated Regression Results

Variable	Coefficient (β)	Std. Error	t- Statistic	Sig.
Constant	0.842	0.200	4.21	0.000
ROA	3.156	0.538	5.87	0.000
Institutional Ownership	1.274	0.520	2.45	0.015
ROA \times GCG	2.018	0.558	3.62	0.001
R ²	0.49			
Adjusted R ²	0.47			
F-statistic	39.82			0.000

Table 5 shows the results of the moderated regression analysis. ROA has a positive and significant effect on firm value, indicating that higher financial performance increases PBV. Institutional ownership also positively affects firm value. Most importantly, the interaction term between ROA and GCG is positive and statistically significant, confirming that Good Corporate Governance strengthens the relationship between financial performance and firm value. The adjusted R² of 47% indicates a strong explanatory power of the model.

Moderating Effect Visualization

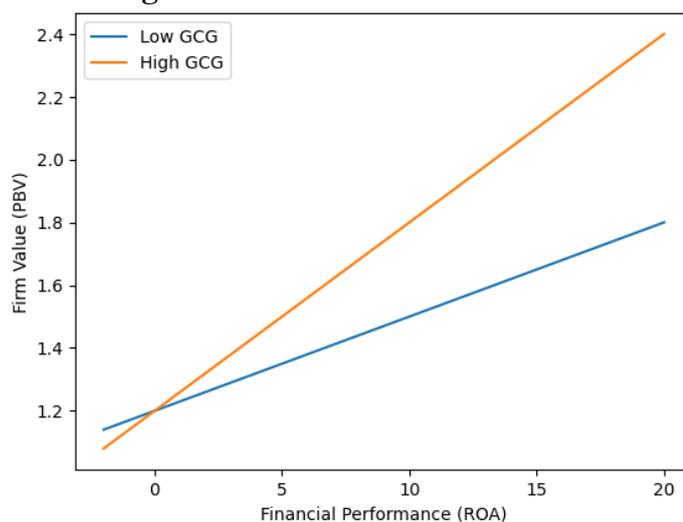


Figure 1. Interaction Effect of GCG on Financial Performance and Firm Value

Figure 1 illustrates the moderating effect of Good Corporate Governance. Firms with

high institutional ownership show a steeper increase in firm value as financial performance improves, compared to firms with low governance quality. This visualization supports the statistical findings of the moderated regression analysis.

Hypothesis Testing Summary

Table 6. Summary of Hypothesis Testing

Hypothesis	Description	Result
H1	Financial performance positively affects firm value	Supported
H2	Good Corporate Governance positively affects firm value	Supported
H3	Good Corporate Governance moderates the effect of financial performance on firm value	Supported

All hypotheses are empirically supported. The results confirm that financial performance and Good Corporate Governance independently influence firm value, and that GCG strengthens the impact of financial performance on firm value.

Discussion

This study investigates the role of Good Corporate Governance (GCG) in moderating the effect of financial performance on firm value in manufacturing companies listed on the Indonesia Stock Exchange. The discussion is structured according to the research hypotheses and integrates empirical findings with relevant theories and prior empirical evidence.

The Effect of Financial Performance on Firm Value

The results indicate that financial performance, measured by Return on Assets (ROA), has a positive and significant effect on firm value, proxied by Price to Book Value (PBV). This finding suggests that manufacturing firms with higher profitability tend to be more highly valued by the market. From the perspective of **Signaling Theory**, profitability serves as a credible signal to investors regarding managerial efficiency and the firm's ability to generate future cash flows. As a result, higher ROA leads to increased investor demand for shares, which ultimately raises firm value.

This finding is consistent with **Agency Theory**, which posits that improved financial performance reflects effective managerial decision-making aligned with shareholders' interests (Jensen & Meckling, 1976). Empirically, this result aligns with previous studies conducted in the Indonesian capital market, which report a positive relationship between profitability and firm value (Pramesti & Rita, 2024; Susanti et al., 2025). Therefore, the first hypothesis stating that financial performance positively affects firm value is empirically supported.

The Effect of Good Corporate Governance on Firm Value

The empirical results also show that Good Corporate Governance, proxied by institutional ownership, has a positive and significant effect on firm value. This indicates that firms with higher institutional ownership tend to have higher market valuations. Institutional

investors generally possess greater monitoring capabilities, which reduces opportunistic managerial behavior and mitigates agency conflicts.

From an agency perspective, strong governance mechanisms enhance oversight and discipline managerial actions, leading to improved corporate credibility in the eyes of investors. This finding supports prior empirical evidence suggesting that governance mechanisms play a critical role in strengthening firm value by increasing transparency and accountability (Andayu, 2025; Cahyani & Kusmayadi, 2025). Thus, Good Corporate Governance functions not only as a control mechanism but also as a value-enhancing factor in the capital market.

The Moderating Role of Good Corporate Governance

The most important finding of this study is the significant moderating effect of Good Corporate Governance on the relationship between financial performance and firm value. The positive and significant interaction term between ROA and GCG indicates that Good Corporate Governance strengthens the impact of financial performance on firm value. This means that profitability contributes more strongly to firm value when supported by effective governance structures.

The interaction plot presented in Figure 1 further confirms this finding, showing that firms with high GCG experience a steeper increase in firm value as financial performance improves compared to firms with low GCG. This result supports the argument that governance mechanisms enhance the credibility of financial information, thereby reinforcing investors' responses to firm performance.

This finding is consistent with **Agency Theory**, which emphasizes that governance mechanisms reduce information asymmetry and agency costs, allowing firms to better translate financial performance into market value. Moreover, from a **Signaling Theory** perspective, strong corporate governance serves as a positive signal that strengthens the market's interpretation of profitability indicators. These results align with previous empirical studies that identify Good Corporate Governance as a moderating variable in the relationship between financial performance and firm value (Andayu, 2025; Susanti et al., 2025).

Implications of the Findings

The findings of this study have both theoretical and practical implications. Theoretically, this study extends the literature on firm value by confirming that Good Corporate Governance acts as a moderating variable rather than merely an independent determinant. This reinforces the integration of Agency Theory and Signaling Theory in explaining firm value formation.

Practically, the results suggest that managers of manufacturing companies should not rely solely on improving financial performance but also focus on strengthening governance mechanisms. Enhancing institutional ownership and governance quality can help firms maximize the positive impact of financial performance on firm value. For investors, the findings highlight the importance of considering governance quality when evaluating firm performance and investment decisions.

Comparison with Previous Studies

Overall, the results of this study are consistent with prior empirical research conducted in Indonesia and other emerging markets. Similar to the findings of Cahyani and Kusmayadi (2025), this study confirms that governance mechanisms enhance firm value formation.

However, this study contributes additional insight by demonstrating that Good Corporate Governance strengthens the relationship between financial performance

CONCLUSION

This study examines the role of Good Corporate Governance in moderating the relationship between financial performance and firm value in manufacturing companies listed on the Indonesia Stock Exchange. The empirical results demonstrate that financial performance, measured by Return on Assets, has a positive and significant effect on firm value. In addition, Good Corporate Governance, proxied by institutional ownership, directly enhances firm value. Most importantly, the findings confirm that Good Corporate Governance strengthens the positive impact of financial performance on firm value, indicating that profitability is more effectively translated into higher market valuation when supported by strong governance mechanisms.

These findings contribute to the literature by reinforcing the integration of Agency Theory and Signaling Theory in explaining firm value formation. From a practical perspective, the results suggest that company management should focus not only on improving financial performance but also on strengthening corporate governance practices to maximize firm value. For investors, governance quality should be considered a key factor when evaluating firm performance and making investment decisions. Overall, this study highlights the strategic importance of Good Corporate Governance in enhancing the market's response to corporate financial performance.

LIMITATION & FURTHER RESEARCH

Future studies are encouraged to expand the scope of this research by including companies from different industrial sectors and extending the observation period to capture long-term governance dynamics. Additionally, future research may employ alternative measures of financial performance and incorporate broader corporate governance proxies, such as board characteristics, audit committee effectiveness, and ownership concentration, to provide a more comprehensive assessment of governance quality. The use of mixed-method or qualitative approaches could also offer deeper insights into how governance mechanisms influence firm value beyond what can be captured through quantitative analysis alone.

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