The Role of Political Connections in Moderating Profitability, Leverage, and Institutional Ownership on Firm Value: Empirical Evidence from the Indonesian Banking Industry

Yuli [1*], Anwar Azazi [2], Anggraini Syahputri [3], Mustarudin [4], Wendy [5]

[1*,2,3,4,5] Faculty of Economics and Business, Tanjungpura University, Indonesia

Email: b1021221141@student.untan.ac.id[1] , anwar.azazi@ekonomi.untan.ac.id[2], anggrainisyahputri@ekonomi.untan.ac.id[3] , mustaruddin@ekonomi.untan.ac.id[4] , wendy@ekonomi.untan.ac.id[5]*

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Abstract

This study aims to analyze the effect of political connections, profitability, and leverage on firm value in banking companies listed on the Indonesia Stock Exchange for the period 2019–2024, with institutional ownership acting as a moderating variable. The research sample consisted of 39 companies with a total of 234 observations selected through purposive sampling, using secondary data sourced from financial reports and share ownership information. The analysis was conducted using Moderated Regression Analysis (MRA) based on panel data. The results show that internal company determinants have an impact on firm value with varying intensity, while political connections are proven to play a selective role in moderating this relationship. These findings contribute to enriching the literature on firm value determinants in the banking sector and governance implications in a highly regulated industry.

INTRODUCTION

Historical performance data for the banking index reported by Investing.com (2025) shows the dynamics of the Indonesian banking sector's performance throughout the 2019–2024 period. The movement of this index reflects changes in macroeconomic conditions, monetary policy, and investor confidence in the banking sector. Fluctuations in the banking sector's performance have a direct impact on firm value, as changes in the index reflect market perceptions of management performance and bank financial stability. This condition encourages banks to improve operational efficiency, maintain asset quality, and strengthen corporate governance in order to maintain firm value and investor confidence. The movement of the Indonesian banking index during the 2019–2024 period is shown in the figure below.

Figure 1. Movement of the Banking Index for the Period 2019–2024
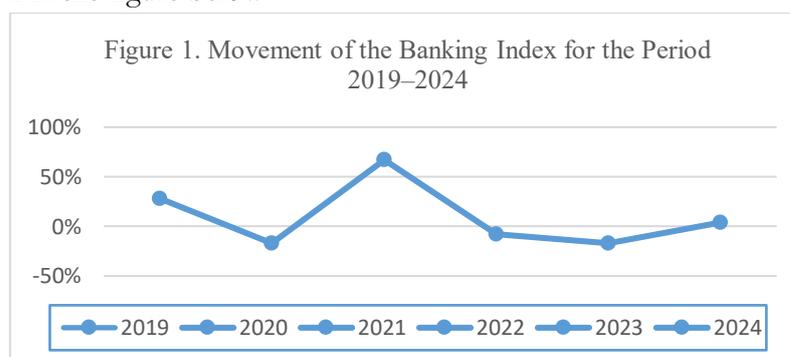
Source: Investing.com, 2025

Based on Figure 1.1, the movement of the Banking Index during the 2019–2024 period shows significant fluctuations and reflects the dynamics of firm value in the banking sector. In

2019, the index grew by 28%, then experienced a sharp contraction of -18% in 2020 as a result of economic pressures triggered by the COVID-19 pandemic. Entering 2021, the index jumped significantly by 67%, reflecting recovery and increased market optimism, but weakened again by -8% in 2022 and contracted further by -17% in 2023. In 2024, the index showed improvement with a growth of 4%, although its movement was still in a fluctuating trend. The fluctuation of the banking index indicates that the firm value of the banking sector is highly responsive to changes in external conditions and internal characteristics of the company. This condition shows that there are specific factors, both external, such as political connections, and internal, such as profitability and leverage, that have the potential to influence the dynamics of firm value. Therefore, empirical testing is needed to identify the main determinants that play a role in shaping banking firm value in Indonesia.

Bank firm value is an important indicator for investors because it reflects market perceptions of a bank's performance and stability. The phenomenon of surging values of digital banks such as ARTO and BBYB in 2020–2022, as well as the consistency of large banks such as BCA, BRI, Mandiri, and BNI, shows that company value is not only influenced by financial performance, but also by market perceptions of business strategies and risks (CNBC Indonesia, 2023).

Bank firm value is also determined by internal company factors, one of which is the level of profitability. Based on banking industry data, Return on Assets (ROA) showed significant fluctuations during 2019–2024. In 2019, banking ROA reached 2.60%, then experienced a sharp decline in 2020 to 1.59% as a direct impact of the COVID-19 pandemic. Subsequently, profitability began to gradually recover in 2021, with ROA increasing to 1.85%, and continued to rise in 2022 to 2.45%. The recovery trend persisted in 2023, with ROA reaching 2.78%, before slightly correcting yet remaining at a relatively high level of 2.72% in 2024 (OJK, 2024). This condition indicates the banking sector's ability to optimize asset management effectively, thereby potentially enhancing investor confidence and increasing firm value. In addition, another internal factor that plays a role in determining firm value is leverage. The high level of leverage in the banking sector, resulting from dependence on third-party funds, is reflected in Bank Panin's Debt to Equity Ratio (DER), which reached 341.17% in 2023 (CNBC Indonesia, 2023). A high leverage ratio may potentially influence investors' perceptions of firm value.

In addition to profitability and leverage, the ownership structure of the banking sector in Indonesia is also dominated by institutional investors. This is reflected in the level of institutional ownership, which reached 11.89% at Bank Mandiri and 8.22% at Bank BRI. A high level of institutional ownership indicates a strong monitoring function within the highly regulated banking industry, thereby potentially influencing the quality of corporate governance and firm value (Mandiri, 2025; BRI, 2025). Thus, political connection, profitability, leverage, and institutional ownership are considered important factors that are believed to play a role in shaping the firm value of banking companies in Indonesia. One external dynamic that may influence investors' assessment of banking firm value is political connection. Political connection is reflected in the involvement of political figures within the board of commissioners of banking institutions, which may affect market perceptions and increase corporate governance risks, particularly in the highly regulated banking industry (Bloomberg, 2025; Republika, 2025).

Firm value can be influenced by internal factors such as profitability, leverage, and institutional ownership, which reflect a company's capacity to generate profits, manage its capital structure efficiently, and strengthen managerial oversight (Anggelita *et al.*, 2025; S. Sembiring & Trisnawati, 2019). Firm value represents investors' perceptions of a company's success (Jihadi *et*

al., 2021). In the banking context, firm value reflects market confidence in a bank's stability and financial performance, as failure to maintain such value may reduce the trust of customers and investors (Wiadnyani & Artini, 2023). The measurement of firm value is commonly proxied by Tobin's Q, which illustrates investors' assessments of company performance as well as management effectiveness in managing corporate assets (Wolfe, 2003). From a managerial perspective, enhancing firm value is a primary corporate objective because it indicates management's success in maximizing shareholder wealth (Wiadnyani & Artini, 2023).

Internal factors such as profitability play a crucial role in determining firm value, as they reflect a company's ability to optimize the use of resources efficiently in generating profits (Brigham & Houston, 2019). Profitability is a financial ratio that indicates the net income earned as a result of the company's financing and operational policies. In this study, profitability is measured using Return on Assets (ROA), as this indicator reflects management effectiveness in utilizing company assets to generate profits efficiently (Markonah *et al.*, 2020). The findings of Anggelita *et al.* (2025) demonstrate that profitability has a positive and significant effect on firm value, as improvements in a company's profit-generating performance directly enhance firm value from investors' perspectives.

Another internal factor that influences firm value is leverage, which reflects the extent to which borrowed funds are used in a company's capital structure. A high level of leverage indicates greater financial risk; therefore, management must carefully balance its benefits and risks ((Tiasrini & Utiyati, 2020). In the banking context, leverage represents the utilization of funds collected from the public such as demand deposits, savings, and time deposits to finance the bank's productive assets. The efficient use of third-party funds (DPK) can increase net interest income and strengthen firm value (Alghifari *et al.*, 2022). This study adopts the Debt to Equity Ratio (DER) as a proxy for leverage, as it reflects the capacity of shareholders' equity to cover the company's total liabilities in the event of a decline in business performance (S. B. Sembiring *et al.*, 2025). Previous studies indicate that leverage is associated with firm value; however, the direction and significance of this relationship remain mixed.

In addition to leverage, another internal factor that plays a role in determining firm value is ownership structure, particularly institutional ownership. Institutional ownership refers to the proportion of shares held by institutions such as banks, insurance companies, and investment institutions (S. Sembiring & Trisnawati, 2019). Institutional ownership functions as a monitoring mechanism that mitigates agency conflicts through oversight of managerial performance (Sholikhah *et al.*, 2024). In the banking sector, this monitoring role becomes even more crucial, as institutions such as banks and pension funds possess greater capacity to influence and control management, thereby potentially enhancing firm value through more effective supervision (Muzakir, 2022). Barrese *et al.* (2025) further emphasize that institutional ownership has a significant positive impact on firm value, indicating that an increase in institutional ownership is accompanied by an increase in firm value.

However, the influence of internal factors on firm value is not always consistent, as it may be affected by external company factors. In this study, political connection is explicitly positioned as a moderating variable that can strengthen or weaken the relationship between profitability, leverage, and institutional ownership and firm value. Political connection is viewed as a double-edged sword because it has the potential both to enhance firm value and to generate risks (Joseline *et al.*, 2021). On the one hand, political connection provides advantages such as easier access to credit, government contracts, and regulatory protection. On the other hand, it may create

corporate governance risks (Faccio, 2006, 2010). In the highly regulated banking sector, political connection may offer strategic benefits, including access to funding and licensing, but it may also increase reputational risk (Faccio, 2006, 2010). Cahyaningtyas *et al.* (2023) found that political connection is able to moderate the effect of financial performance on firm value; however, it does not moderate the relationship between institutional ownership and firm value. This suggests that the effectiveness of political connection as a moderating variable is selective and depends on the specific internal variables being examined.

In addition to the main and moderating variables, this study also incorporates firm size and the crisis period (COVID-19) as control variables to improve the accuracy of the estimation. Firm size is proxied by the natural logarithm of total assets; thus, firm size is determined based on the natural log value of a bank's total assets. Meanwhile, the COVID-19 crisis period is measured using a dummy variable, assigning a value of 1 to the period during which the COVID-19 crisis occurred and 0 to periods outside the crisis (Perwitasari *et al.*, 2022). The inclusion of these two control variables allows differences in operational scale and economic conditions during the crisis period to be accounted for, thereby enabling the effects of the main variables on firm value to be estimated more objectively and accurately.

This study is grounded in signaling theory and agency theory to explain the influence of external and internal factors on firm value. Signaling theory, proposed by Spence (1973) suggests that profitability serves as a performance signal conveyed by a company to investors, where a high level of profitability is perceived as a positive signal that can enhance firm value. Meanwhile, agency theory, introduced by Jensen & Meckling (1976) explains that the relationship between management and investors may give rise to agency conflicts due to differences in interests and information asymmetry. From this perspective, leverage as an internal factor reflects the company's capital structure, which may function as a disciplinary mechanism due to debt repayment obligations, but may also increase financial risk if not managed optimally. Institutional ownership acts as a monitoring mechanism to reduce agency conflicts. Political connection is positioned as a moderating variable that can either strengthen or weaken the influence of profitability, leverage, and institutional ownership on firm value. It operates through a dual effect: providing access to strategic resources and regulatory advantages, while simultaneously potentially increasing conflicts of interest that may affect market perceptions (Faccio, 2010).

The inconsistency of empirical findings regarding the effects of profitability, leverage, and institutional ownership on firm value in the Indonesian banking sector during the 2019–2024 period indicates the need for further research to obtain more consistent results. These differences in findings are suspected to be influenced by political connection, which in this study is positioned as a moderating variable. In line with the above discussion, this study proposes the following research questions: Does profitability (ROA) affect firm value?; Does leverage (DER) affect firm value?; Does institutional ownership (IO) affect firm value?; Is political connection (PC) able to moderate the influence of these three variables on firm value? Therefore, this research is important to conduct in order to provide more comprehensive empirical evidence and to strengthen the understanding of the determinants of firm value in the banking sector.

Based on the inconsistency of previous empirical findings, this study aims to analyze the effects of profitability, leverage, and institutional ownership on firm value in the Indonesian banking sector during the 2019–2024 period, as well as to examine the role of political connection as a moderating variable in these relationships.

METHODS

This study employs a quantitative method with a causal-associative research design to examine the impact of of profitability, leverage, and institutional ownership on firm value, while considering political connection as moderating variable. The research subjects consist of 47 banks listed on the Indonesia Stock Exchange (IDX) as of the end of 2024. The sample was selected using purposive sampling based on specific criteria, namely: (1) banks that were listed on the IDX during the 2019–2024 period. Based on these criteria, 39 banks were selected as the final sample. With a six-year observation period, the total number of observations amounts to 234 (39 banks multiplied by 6 years). The data used in this study are secondary data obtained from annual financial reports, share ownership structures, profiles of board of commissioners members, and stock price data, accessed through the official IDX portal and the respective companies' websites.

Data analysis was conducted using Moderated Regression Analysis (MRA) based on panel data to examine the effects of profitability, leverage, and institutional ownership on firm value, with political connection as a moderating variable. The data were processed using EViews 12 software. The analysis began with descriptive statistics, including the mean, minimum, maximum, and standard deviation values. This was followed by the selection of the most appropriate panel data model through the Chow test and the Hausman test to determine whether the common effect, fixed effect, or random effect model was the best fit. Subsequently, classical assumption tests were performed, including tests for multicollinearity and heteroskedasticity. Finally, hypothesis testing and the estimation of moderating effects were conducted by incorporating interaction variables into the regression model.

RESULTS AND DISCUSSION

This section presents the empirical analysis results concerning the effects of political connection, profitability, and leverage on firm value in the banking sector, as well as the role of institutional ownership as a moderating variable. The analysis begins with the presentation of descriptive statistics to explain the characteristics of the research data, followed by the determination of the most appropriate panel data regression model and hypothesis testing. Subsequently, the research findings are interpreted by linking the empirical results to the relevant theoretical framework and prior studies.

Descriptive Statistics

Table 1. Descriptive Statistics

	FV	ROA	DER	IO	PC	FS	KRIS
Minimum	0.159	-8.699	0.192	39.612	0.000	28.558	0.000
Maximum	10.665	5.671	16.078	99.999	1.000	35.425	1.000
Mean	1.176	0.676	5.176	91.150	0.232	31.702	0.333
Std. Dev	1.053	1.741	2.803	10.103	0.240	1.688	0.472
Observasi	234	234	234	234	234	234	234

Source: Processed using EViews 12, 2026

Based on the descriptive statistics results, the firm value (FV) variable shows a minimum value of 0.348 and a maximum of 2.786, with a mean of 1.041 and a standard deviation of 0.294, indicating moderate variation across companies. The political connection (PC) variable ranges from 0.000 to 1.000, with a mean of 0.215 and a standard deviation of 0.232, suggesting that political connections are unevenly distributed among the sampled firms. Profitability, measured by return on assets (ROA), ranges from -0.089 to 0.090, with a mean of 0.007 and a standard deviation of 0.020, reflecting relatively low profitability levels and limited variation. The leverage variable (DER) has a minimum value of 0.303 and a maximum of 11.330, with a mean of 4.936 and a standard deviation of 2.402, indicating significant differences in debt utilization among companies. Institutional ownership (IO) shows a minimum value of 0.396 and a maximum of 0.999, with a mean of 0.914 and a standard deviation of 0.101, suggesting a generally high and relatively homogeneous level of institutional ownership. Firm size (FS) ranges from 28.945 to 35.425, with a mean of 31.742 and a standard deviation of 1.631, indicating variation in company size within the sample. The crisis variable (KRIS) ranges from 0.000 to 1.000, with a mean of 0.333 and a standard deviation of 0.472, indicating that approximately one-third of the observations occurred during the crisis period.

Model Selection

Table 2. Model Selection

Model	Uji Chow	Uji Hausman	Hasil
Model 1	Prob 0.000 < 0.05	Prob. 0.0002 < 0.05	FEM
Model 2	Prob 0.000 < 0.05	Prob. 0.0009 < 0.05	FEM
Model 3	Prob. 0.000 < 0.05	Prob. 0.0000 < 0.05	FEM

Source: Processed using EViews 12, 2026

The model selection test presented in the table above indicates that for Model 1, Model 2, and Model 3 regressions, based on the results of the Chow test and the Hausman test, the Fixed Effect Model (FEM) is the most appropriate panel data regression model for this study.

Classical Assumption Tests

The classical assumption tests in the Fixed Effect Model (FEM) include the multicollinearity test and the heteroskedasticity test (R. B. Napitupulu et al., 202

Table 3. Classical Assumption Tests

Variabel	Multikolinieritas					Heteroskedastisitas	
	ROA	DER	IO	FS	KRIS	Prob F-statistic	Prob Chi-Square
ROA	1.0000	-0.1394	0.3206	0.3633	-0.1175		
DER	-0.1394	1.0000	-0.2022	0.2948	0.0826		
IO	0.3206	-0.2022	1.0000	0.2963	-0.0524	0,4559	0,4538
FS	0.3633	0.2948	0.2963	1.0000	-0.0416		
KRIS	-0.1175	0.0826	-0.0524	-0.0416	1.0000		

Source: Processed using EViews 12, 2026

Based on the results of the classical assumption tests, the model meets the required criteria. The multicollinearity test shows that the correlation coefficients among the independent variables ROA, DER, IO, FS, and KRIS are all below 0.80, indicating that there is no high correlation among the independent variables and, therefore, no multicollinearity problem in the model (R. B. Napitupulu et al., 2021). Furthermore, the heteroskedasticity test using the ARCH test produces a Prob. F-statistic value of 0.4559 and a Prob. Chi-Square (Obs*R-squared) value of 0.4538, both of which are greater than the 0.05 significance level. This indicates that the regression model does not exhibit heteroskedasticity and satisfies the assumption of

homoskedasticity, making it appropriate for further analysis (R. B. Napitupulu et al., 2021).

Hypothesis Testing

Table 4.4. Hypothesis Testing

Model	Variabel	Koefisien (β)	Std. Error	t-Statistik	Prob
	Constant	-2.4101	0.9716	-2.4803	0.0140
	ROA	0.1032	0.0486	2.1234	0.0350
	DER	0.1629	0.0432	3.7647	0.0002
	IO	0.0293	0.0093	3.1234	0.0021
			Effect Specification		
1	R-Squared	0.573090	Mean dependent var		1.176435
	Adjusted R-Square	0.481927	S.D. dependent var		1.053291
	S.E. of regression	0.758103	Akaiko info criterion		2.445226
	Sum squared resid	110.3543	Schwarz criterion		3.065412
	Log likehood	-244.0915	Hanan-Quinn criter.		2.695285
	F-Statistic	6.286423	Durbin-Watson stat		2.415506
	Prob (F-Statistic)	0.000000			
	Constant	-10.8723	6.2484	-1.7400	0.0835
	ROA	0.0938	0.0513	1.8277	0.0692
	DER	0.1685	0.0454	3.7092	0.0003
	IO	0.0308	0.0095	3.2447	0.0014
	PC	-0.1403	0.5052	-0.2778	0.7814
	FS	0.2620	0.1898	1.3800	0.1692
	KRIS	0.0672	0.1113	0.6040	0.5465
2			Weight Statistics		
	R-Squared	0.577725	Mean dependent var		1.176435
	Adjusted R-Square	0.479418	S.D. dependent var		1.053291
	S.E. of regression	0.759964	Akaiko info criterion		2.459950
	Sum squared resid	109.1560	Schwarz criterion		3.124435
	Log likehood	-242.8141	Hanan-Quinn criter.		2.727870
	F-Statistic	5.876725	Durbin-Watson stat		2.424477
	Prob (F-Statistic)	0.000000			
	Constant	-4.4266	5.9558	-0.7432	0.4583
	ROA	0.2938	0.0664	4.4248	0.0000
	DER	0.0456	0.0575	0.7931	0.4287
	IO	0.0197	0.0098	2.0080	0.0461
	PC	-0.8421	3.0026	-0.2804	0.7794
	ROA*PC	-0.7967	0.1764	-4.5164	0.0000
	DER*PC	0.4662	0.1283	3.6330	0.0004
	IO*PC	-0.0173	0.0335	-0.5176	0.6053
	FS	0.1082	0.1800	0.6009	0.5486
3	KRIS	-0.0076	0.1039	-0.0734	0.9415
			Weight Statistics		
	R-Squared	0.644817	Mean dependent var		1.176435
	Adjusted R-Square	0.555066	S.D. dependent var		1.053291
	S.E. of regression	0.702580	Akaiko info criterion		2.312568
	Sum squared resid	91.81315	Schwarz criterion		3.021352
	Log likehood	-222.5704	Hanan-Quinn criter.		2.598349
	F-Statistic	7.184546	Durbin-Watson stat		2.291337
	Prob (F-Statistic)	0.000000			

Source: Processed using EViews 12, 2026

1. Panel Data Regression Analysis

This study employs panel data regression analysis using the Moderated Regression Analysis (MRA) approach. Panel data regression is used to examine the effect of independent variables on the dependent variable by considering both time-series and cross-sectional dimensions. Model 3 represents the moderating model, which tests whether political connection strengthens or weakens the relationships between ROA, DER, institutional ownership, and firm value.

Based on the estimation results, the regression equation for Model 1 is as follows:

FV = -2.4101 + 0.1032ROA + 0.1629DER + 0.0293IO + e

The constant value of -2.4101 indicates that when ROA, DER, and IO are assumed to be constant, firm value equals -2.4101. The ROA coefficient of 0.1032 implies that a one-unit increase in ROA increases firm value by 0.1032, holding other variables constant. The DER coefficient of 0.1629 indicates that a one-unit increase in DER increases firm value by 0.1629. Meanwhile, the IO coefficient of 0.0293 shows that a one-unit increase in institutional ownership increases firm value by 0.0293.

The regression equation for Model 2 is as follows:

FV = -10.8723 + 0.0938ROA + 0.1685DER + 0.0308IO − 0.1403PC + 0.2620FS + 0.0672KRIS + e

The constant value of -10.8723 indicates that when all independent and control variables are held constant, firm value equals -10.8723. The coefficients of ROA (0.0938), DER (0.1685), and IO (0.0308) show positive relationships with firm value. Political connection has a coefficient of -0.1403, indicating a negative relationship with firm value. Firm size (FS), with a coefficient of 0.2620, suggests that larger firms tend to have higher firm value. The crisis variable (KRIS) has a coefficient of 0.0672, indicating a positive association with firm value.

In Model 3, interaction variables are added to test the moderating effect, resulting in the following equation:

FV = -4.4266 + 0.2938ROA + 0.0456DER + 0.0197IO − 0.8421PC − 0.7967(ROA×PC) + 0.4662(DER×PC) − 0.0173(IO×PC) + 0.1082FS − 0.0076KRIS + e

The constant value of -4.4266 indicates that when all independent variables are held constant, firm value equals -4.4266. The ROA coefficient of 0.2938 implies that a one-unit increase in ROA increases firm value by 0.2938, ceteris paribus. The DER coefficient of 0.0456 indicates that a one-unit increase in DER increases firm value by 0.0456. The IO coefficient of 0.0197 suggests that a one-unit increase in institutional ownership increases firm value by 0.0197. Regarding the interaction terms, the ROA×PC coefficient of -0.7967 indicates that political connection weakens the effect of ROA on firm value. In contrast, the DER×PC coefficient of 0.4662 shows that political connection strengthens the effect of DER on firm value. Meanwhile, the IO×PC coefficient of -0.0173 suggests that political connection does not significantly strengthen or weaken the relationship between institutional ownership and firm value.

The changes in coefficients after including interaction terms reflect the implications of moderation analysis as explained by Baron and Kenny (1986), where the effect of independent variables on the dependent variable becomes conditional. In models containing interaction terms, the main variable coefficients no longer represent a general direct effect, but rather the effect when the moderating variable equals zero. Therefore, changes in the magnitude or direction of coefficients are a normal methodological consequence in moderation analysis.

The t-test is used to examine the hypothesis regarding the partial effect of independent variables on the dependent variable. If the probability value is less than 0.05, the hypothesis is accepted, indicating that the independent variable has a significant effect on the dependent variable (R. B. Napitupulu et al., 2021).

2.   t-Test

The t-test results indicate that in Model 1, ROA, DER, and institutional ownership (IO) have positive and significant effects on firm value. In Model 2, DER and IO remain positive and significant, while ROA, political connection (PC), firm size (FS), and crisis (KRIS) are not significant. In Model 3, ROA and IO show positive and significant effects, whereas DER is not significant. The interaction terms ROA×PC and DER×PC are significant, indicating that political

connection moderates the effects of ROA and DER on firm value, while IO×PC is not significant. Additionally, the control variables FS and KRIS are not significant in Model 3.

3. Coefficient of Determination Test (Adjusted R-Square)

The coefficient of determination test shows that Model 1 has an Adjusted R-Square of 0.481927, indicating that ROA, DER, and institutional ownership explain 48.19% of the variation in firm value. Model 2 produces an Adjusted R-Square of 0.479418, meaning that the inclusion of political connection and control variables explains 47.94% of the variation. Meanwhile, Model 3 shows an increased Adjusted R-Square of 0.555066, indicating that after adding the interaction terms, the model explains 55.51% of the variation in firm value. This improvement suggests that the moderating model has stronger explanatory power compared to the previous models.

4. MRA Interaction Test (Moderated Regression Analysis)

The moderation test is conducted to determine whether political connection is able to strengthen or weaken the relationship between the independent variables and the dependent variable by incorporating interaction terms into the regression model (Cahyaningtyas et al., 2023). Based on the test results, the interaction terms ROA×PC and DER×PC are statistically significant, whereas the interaction term IO×PC is not significant. This indicates that political connection moderates the relationship between ROA and firm value as well as between DER and firm value, but does not moderate the relationship between institutional ownership and firm value. Furthermore, since political connection remains included in the regression model as an independent variable, even though it is not directly significant, it can be categorized as a quasi-moderator. A quasi-moderator is a variable that functions as a moderator while simultaneously remaining part of the main regression model Baron & Kenny (1986).

DISCUSSION

Profitability on Firm Value

The analysis results indicate that profitability, proxied by Return on Assets (ROA), has a positive and significant effect on firm value ($\beta = 0.1032$; $p = 0.0350$). Therefore, the first hypothesis (H1), which states that profitability positively affects firm value, is accepted. This finding suggests that the profit level of banking firms is an important determinant in shaping firm value from investors' perspectives (Widiantari et al., 2025). Based on signaling theory (Spence, 1973), profitability serves as a positive signal regarding company performance quality and future prospects, as a high ROA reflects efficiency in managing assets to generate profits, thereby increasing market confidence. In the highly regulated banking industry, profitability remains a key indicator of financial health, as it reflects effective management of productive assets and operational stability (Wiadnyani & Artini, 2023).

However, after incorporating control variables—firm size and crisis conditions—in Model 2, profitability no longer shows a significant effect on firm value ($\beta = 0.0938$; $p = 0.0692$), although the direction remains positive. This suggests that the sensitivity of ROA's effect on firm value is influenced by structural and macroeconomic factors. Theoretically, during crisis periods or when firm size is considered, investors do not focus solely on current profitability but also on resilience, business diversification, and asset strength, which are generally more prominent in larger banks. Thus, profitability becomes less dominant as a single determinant of firm value because the market also considers systemic risk and long-term stability (Wiadnyani & Artini, 2023). Nevertheless, the consistently positive coefficient indicates that profitability still plays an economic role in enhancing firm value, although its influence is not entirely independent of

company characteristics and economic conditions. These findings are consistent with (Halawa *et al.*, 2024) and (S. B. Sembiring *et al.*, 2025), which confirm that profitability positively affects firm value.

Leverage on Firm Value

The analysis further shows that leverage, proxied by the Debt to Equity Ratio (DER), has a positive and significant effect on firm value (β = 0.1629; p = 0.0002). Thus, the second hypothesis (H2), which states that leverage affects firm value, is accepted. This finding indicates that an increase in leverage can enhance firm value. According to agency theory (Jensen & Meckling, 1976), debt functions not only as a source of financing but also as a disciplinary mechanism that limits managerial opportunism through mandatory interest and principal payments, thereby creating external pressure and strengthening monitoring by creditors (Halawa et al., 2024).

In the banking context, although leverage is inherent due to third-party funds being classified as liabilities, the market evaluates how effectively such debt is managed (Sholikhah et al., 2024). Controlled leverage is perceived as a strategic tool for expansion and risk management, reflecting a balance between risk and return. After adding firm size and crisis conditions as control variables in Model 2, leverage remains positive and significant (β = 0.1685; p = 0.0003), indicating that its effect is consistent and robust even after accounting for firm characteristics and macroeconomic conditions. Therefore, an optimal debt-based financing structure remains a stable factor in increasing firm value, supporting the findings of Halawa et al. (2024) dan S. B. Sembiring et al. (2025) that leverage positively influences firm value within optimal limits.

Institutional Ownership on Firm Value

The analysis results indicate that institutional ownership (IO) has a positive and significant effect on firm value; therefore, the third hypothesis (H3) is accepted. This finding implies that a higher proportion of institutional ownership leads to higher firm value. In line with agency theory proposed by Jensen and Meckling (1976), institutional ownership functions as a strong monitoring mechanism over management. Unlike individual investors, institutional investors possess greater resources, analytical expertise, and substantial economic interests, which motivate them to conduct active monitoring, demand transparency, and ensure that managerial decisions align with shareholders' interests (Anggelita et al., 2025). Consequently, higher institutional ownership reduces agency conflicts and improves the quality of strategic decision-making, which is ultimately reflected in increased firm value.

Beyond its monitoring role, institutional ownership also enhances corporate governance legitimacy in the eyes of the market. A high level of institutional ownership signals that the company has passed rigorous evaluation and selection processes by professional investors, thereby creating reputational effects and strengthening investor confidence. In the banking sector—characterized by strict regulation and exposure to systemic risk—the presence of institutional shareholders is particularly crucial in reinforcing managerial discipline, risk oversight, and regulatory compliance. These findings are consistent with Holly *et al.* (2021) and Pratama *et al.* (2021), who argue that institutional ownership is an effective governance mechanism in enhancing firm value, particularly in complex and highly regulated industries such as banking.

Political Connection Moderates the Effect of Profitability on Firm Value

The analysis further reveals that the interaction between profitability and political connection significantly affects firm value, indicating that political connection acts as a moderating variable in this relationship. The negative direction of the interaction suggests that political

connection weakens the effect of profitability on firm value. According to signaling theory (Spence, 1973), profitability serves as a positive signal to the market because it reflects a company's ability to generate earnings and sustain strong future performance. However, from the perspective of agency theory (Jensen & Meckling, 1976), political connections may increase agency conflicts if such relationships create opportunities for moral hazard, inefficient decision-making, or opportunistic behavior that does not align with shareholders' interests. Investors evaluate not only the magnitude of profits but also their quality and sustainability. In politically connected firms, high profitability may be perceived as resulting from political privileges, preferential treatment, or non-market-based policies, thereby weakening the credibility of profitability as a positive signal. As a result, investors may become more cautious in assessing the quality of reported earnings. Thus, even when a firm demonstrates high profitability, the presence of political connections can reduce the strength of profitability's impact on firm value due to concerns over governance risks and potential agency costs. This finding contradicts Cahyaningtyas et al. (2023), who suggest that political connections strengthen the relationship between profitability and firm value. Instead, the present study indicates that political connection weakens this relationship, implying that the market carefully considers governance risks and potential agency costs when evaluating politically connected firms (Faccio, 2010).

Political Connection Moderates the Effect of Leverage on Firm Value

The analysis indicates that political connection moderates the relationship between leverage and firm value; therefore, the fifth hypothesis (H5) is accepted. The positive and significant interaction coefficient suggests that political connection strengthens the effect of leverage on firm value. From the perspective of agency theory (Jensen & Meckling, 1976), leverage functions as a disciplinary mechanism that reduces managerial opportunism due to mandatory debt obligations, which pressure management to operate more efficiently. When a firm has political connections, external oversight and potential access to policy support may enhance market confidence that leverage is managed prudently rather than excessively increasing risk (Napitupulu & Ermaya, 2025). In the highly regulated banking sector, political connections may provide additional legitimacy and reinforce perceptions of funding stability. As a result, leverage is not viewed solely as a risk factor but also as a credible and well-managed financing strategy when supported by political ties, ultimately contributing to higher firm value. This finding is consistent with (Napitupulu & Ermaya, 2025) and Supatmi et al. (2019), who argue that politically connected firms tend to gain greater legitimacy from investors and creditors, leading debt to be perceived not merely as a source of risk but also as an expansion strategy supported by network access and policy stability.

Political Connection Moderates the Effect of Institutional Ownership on Firm Value

The analysis further shows that political connection does not significantly moderate the relationship between institutional ownership and firm value; therefore, the sixth hypothesis (H6) is rejected. This finding indicates that political connection neither strengthens nor weakens the effect of institutional ownership on banking firm value. According to agency theory (Jensen & Meckling, 1976), institutional ownership already serves as an effective monitoring mechanism in reducing agency conflicts and improving managerial oversight. Since this monitoring function operates independently through institutional investors, political connection does not provide additional moderating influence Agustina et al. (2022). These findings align with Agustina et al. (2022) dan Cahyaningtyas et al. (2023), who state that institutional investors generally possess strong analytical capabilities and a long-term performance orientation. Consequently, their

evaluation of firm value does not depend on the presence or absence of political connections. Thus, the effect of institutional ownership on firm value remains determined by the effectiveness of its monitoring role rather than by political connection as a contextual factor.

CONCLUSION

Institutional ownership is found to be a consistent determinant in enhancing firm value, while profitability has a positive effect whose sensitivity is influenced by firm size and crisis conditions. Political connection plays a selective moderating role: it weakens the effect of profitability on firm value, strengthens the effect of leverage on firm value, and does not moderate the relationship between institutional ownership and firm value. These findings indicate that in the highly regulated banking industry, firm value is determined not only by performance and internal governance mechanisms but also by how the market perceives the political context embedded within the company. Thus, political connection acts as a contextual factor influencing the strength of the relationship between internal variables and firm value.

From a practical perspective, banks are advised to manage leverage optimally and maintain the effectiveness of institutional ownership as a monitoring mechanism to sustainably enhance firm value. Additionally, political connections should be balanced with transparent governance practices to avoid reputational risk perceptions that could weaken firm value. Academically, future research is recommended to expand the research objects and observation periods, incorporate additional governance variables, and employ more comprehensive proxies for political connection in order to provide deeper insights into the moderating role of political ties on the relationship between internal corporate factors and firm value across various industries.
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