The Effect of Financial Ratios and Company Size on Company Financial Performance

Dwi Egalita Novia Maharani Agustin Ekadjaja

Faculty of Economics & Business, Universitas Tarumanagara, West Jakarta - 11470, Indonesia
Corresponding author. Email: agustine@fe.untar.ac.id

Submitted: June 2022, Revised: November 2022, Accepted: February 2023

ABSTRACT
The goal of this study is to learn more about the effect of Total Asset Turnover, Current Ratio, Leverage, and Company Size on Company Financial Performance. This study uses a sample of 26 manufacturing companies in the consumer goods industry during 2017-2020 which can be seen on the IDX obtained using the purposive sampling method. The application used for data processing in this research is E-views 12. This test results that Total Asset Turnover and Company Size have a significant impact on the Financial Results of the Firm, Current Ratio has a negative and insignificant effect on the Firm Performance, and Leverage has a negative significant impact on the Firm Performance. From this research, high-quality management is needed to encourage companies to improve their performance to figure out how to compete with the best strategies and subsequently maintain the Company’s Financial Performance for the survival of the firm.

Keywords: Company Financial Performance, Total Asset Turnover, Current Ratio, Leverage, Company Size

1. INTRODUCTION
In the midst of today's developments, the economic growth of a country has begun to increase from year to year. This growth is indicated by the number of companies competing in a country to get their respective markets with the innovations they create. The increase in the economy of a country will determine the welfare of the people in a country. Competition is very tight, so companies must be able to create opportunities and innovations to increase company revenues. However, during the competition carried out by entrepreneurs, suddenly the world was shocked by a big disaster. Not only Indonesia but all countries were affected by the Corona Virus pandemic in 2019. The state of the economy has declined greatly because the wheels of the economy were almost paralyzed during the pandemic. The pandemic has also resulted in people losing their jobs so people's lifestyles have changed completely. Before the pandemic, people's lifestyles were very consumptive, but for some people, this has changed because many of them do not generate income anymore.

Opportunities are increasingly open for investors to invest their capital. Business people continue to struggle as much as possible to maintain their business so as not to fall even in difficult conditions. These situations and conditions require management to be able to run optimally so that all company activities can be managed and controlled properly to get maximum profit with the aim that activities run as they should.

The pandemic is still ongoing. Covid-19 has had a considerable influence on some businesses, but not all. Several sectors have raised the financial performance so it can help increase economic growth. One of them is a manufacturing company that helps economic growth in Indonesia in the field of consumer products. The consumer products industry has begun to create an industrial branch whose activities include operating equipment, machinery, and labor in the process of turning raw materials, spare parts, and other components into commodities with a market value and ready for public sale. The success of the consumer goods industry sector in
supporting the economy is certainly supported by the financial performance of manufacturing companies. Investors will study the company's financial statements and financial performance before they invest their capital. When the company has good financial performance, the company can provide profits to the owners of capital with a high value, so that investors will be interested in giving their capital.

Although there have been many studies on foreign ownership, the results are still inconsistent. M. Firza and Ade (2018) [1] show that Total Asset Turnover and Current Ratio possess a significant effect on ROA. However, Puji (2020) [2] revealed that there was no significant effect between Total Asset Turnover and the Current Ratio on the Company's Financial Performance. Aamir et al. (2021) [3] revealed that Leverage has a considerable negative impact on firm performance as measured by ROA. However, Yulita et al. (2017) [4] said that from the results of his research it was found that Leverage has a significant effect on Return On Assets. Nasib (2019) [5] shows that the Company’s Size give a significant effect on Financial Performance. However, Thaiba and Faisal (2020) [6] show that Company Size has a positive and insignificant effect on Financial Performance on Company.

1.1. Related Work

According to Brigham and Houston (2014:184) [7], Signaling Theory is a management behavior in a company that provides direction for investors related to management's view of the company for the future. Signals sent through organizations can be both beneficial and bad (Fauziah, 2017) [8]. Signal theory from (Agung, Satria & Madi, 2017) [9] explains that companies provide theories to investors that aim to see the condition and performance of a company. With this theory, the success or failure of a company can be described clearly. According to Kraus and Litzenberger (1973) in Jansen (2014) [10], the Trade-Off theory is separated into two parts, namely Static and Dynamic Trade-Off Theory. Static Trade-Off Theory, says that debt has advantages and disadvantages, whereas the advantage of debt is that companies can make tax savings because interest expense is a tax deduction. Apart from that, debt also has a weakness, namely the risk that the company can go bankrupt.

Investors will use information such as financial statements to observe the performance of a company before they decide to invest in it. Therefore, the presence of this idea, it is anticipated, will reveal information about the company's assets as measured using Return on Assets (ROA) commonly known as the level of assets and it can also be seen whether the amount of profit that can be obtained from the assets used. So, if the Return on Assets (ROA) has a high value, then it gives a good signal for investors. Return On Assets can have a positive influence, namely, investors will trust the company more because Return on Assets (ROA) is considered to have good financial performance so that investors can be sure to invest their capital.

The company's financial performance (Maria, 2019) [11] is the firm's capability to carry out its business which is financially written in the financial statements. In this case, the Financial Performance is proxied using ROA. The Financial Performance is a way to see the success of business activities by predetermined standards and criteria, as well as how the company achieves success with the specified targets so that treatment that is not by the rules can be eliminated by making continuous improvements. Therefore, knowing the condition of the company's performance is very necessary.

Total Asset Turnover (TATO) is the ratio between sales and total assets used for company activities. Total Asset Turnover can be used to assess the efficiency of investment in various assets and can show the ability of the company's assets ability to perform total net sales. This ratio will be able to know the actual performance of management in carrying out company activities. Broadly speaking, this ratio can reveal accounts receivable turnover, what is the average period of collection of accounts receivable, inventory turnover, what is the average time inventory is stored in the warehouse until it is finally sold, working capital turnover, fixed asset turnover, and total asset turnover. The greater the value of this ratio, it can be concluded that the more effective the company is in generating overall net revenues by utilizing its assets. When the company uses its assets effectively by obtaining net sales, then this shows that the financial performance achieved by the company is getting better.

The current ratio measures a company's capacity to repay all of its financial obligations. These obligations are in the form of short or long-term liabilities that are almost close to maturity. This ratio is also known as the liquidity ratio where this ratio acts as a bridge between cash and other current
assets and current liabilities. By dividing current assets by current liabilities or liabilities, the Current Ratio can be calculated. A high current ratio demonstrates that the firm can pay its short-term debt and have adequate assets to ensure the company already has budgeted funds at maturity. This means that the company has good finances, so the company is safe from liquidation. Conversely, if the Current Ratio is low, it means that the company's assets are insufficient to service its short-term debt and is at risk of going bankrupt. The higher the current ratio, the lower the risk of the corporation failing to meet its short-term obligations, the better.

Leverage is the use of funds from a third person (debt) where these funds have a fixed burden that must be repaid by the industry, namely in a form that has the aim of increasing the capital structure of the industry to increase profits for the industry or company and profits for shareholders. A high Leverage value means that the company's debt is also bigger than its capital, so the costs to be paid to fulfill obligations will also be greater. As a result, the firm's profit margins will dwindle. This ratio can provide information about the income of funds used by the company, whether it comes from its capital or comes from debt.

A corporation's size is determined by its total assets. The larger the assets owned by the company, the greater the company's size, and vice versa. When the company has a large size, it is easier for management to use these assets to generate profits. When the company has a large size, it also makes it easier for the company to obtain sources of funds so that the company can more easily develop its company because it has a lot of capital and it will influence the firm performance.

The hypotheses of this research are as follows:

**H1.** Total Asset Turnover has a positive effect on the Company's Financial Performance

**H2.** Current Ratio has a positive effect on the Company's Financial Performance

**H3.** Leverage has a negative effect on the Company's Financial Performance

**H4.** Company size has a positive effect on the Company's Financial Performance

This ratio indicates the ability of the company's assets to obtain total net sales. The higher the total asset turnover ratio of a company, the more effective the company is in using its assets to generate total net sales. When the company can use its assets effectively to generate net sales, this means that the Company's Financial Performance will grow. The bigger this ratio, the better, because it signifies that the assets used to help the company's sales are more efficient and operations to improve the Firm’s Financial Performance. The findings of an investigation conducted by M. Firza Alpi and Ade Gunawan (2018) [1] said in their research that Total Asset Turnover give an effect on ROA. The results of research from Intan, Fery, Yenfi (2017) [12] partially show that between TATO and ROA there is a positive influence.

**H1.** Total Asset Turnover has a positive effect on the Company's Financial Performance

The Current Ratio is the strength of a company to meet short-term commitments for company operations. M. Firza Alpi and Ade Gunawan (2018) [1] the Current Ratio makes an impact on Return on Assets. Maria (2019) [11] also shows the results of her research that the current ratio has a significant positive effect on the Firm Performance.

**H2: Current Ratio has a positive effect on the Company's Financial Performance**

Leverage is the utilization of assets and sources of capital by organizations with fixed costs to boost the potential returns of shareholders. Companies that use debt in financing activities for the company's operational activities not only have a good impact on the company but also have an unfavorable impact. If the proportion of leverage is ignored by the company, it can cause the company's profitability to decrease due to the use of debt which causes a fixed interest expense. Debt that is too high can reduce the excess cash flow so that in the firm Leverage influences the Company's Financial Performance. According to Aamir et al. (2021) [3] and Ilker (2021) [13], they reveal that Leverage give a negative and significant impact on ROA.

**H3: Leverage has a negative effect on the Company's Financial Performance**
The company's size can be considered based on the assets owned by the company. The larger the size of the company, the greater its ability to obtain funding sources, diversify products, conduct research, and so on. When the company has assets that are greater than the assets of other companies, it can be concluded that the company will produce in large quantities. So that it has the opportunity to get profits and it will have an effect on the company's financial results of the company, which is to be even better. Research conducted by Nasib (2019) [5] illustrates that the firm's size provides an impact on the performance of the company, which in this case is the Return on Assets.

**H4:** Company Size has a positive effect on the Company's Financial Performance

### 1.2. Our Contribution

The goal of this research was to find out whether Total Asset Turnover, Current Ratio, Leverage, and Company Size had a significant effect on the Company's Financial Performance.

### 1.3. Paper Structure

This test's technique is quantitative, using secondary data collected from the Indonesia Stock Exchange between 2017-2020. Obtaining the data was used by the purposive sampling technique. In this investigation, the following criteria were used are: (1) Consumer products manufacturing companies are listed on the Indonesia Stock Exchange (IDX) from the 2017-2020 period, (2) Companies that present consistent financial statements ending on 31 December, and (3) Companies that do not experience losses during the 2017-2020 period. This study uses one dependent variable and four variables that are not dependent. The dependent variable of this research is the Company's Financial Performance and the independent variables used are Total Asset Turnover, Current Ratio, Leverage, and Company Size.

### 2. BACKGROUND

ROA is a statistic for evaluating a company's performance that is calculated by dividing total net income by total assets. The Total Asset Turnover variable is measured by dividing Sales by Total Assets, the Current Ratio is calculated by dividing Current Assets by Current Liabilities, Total Liabilities divided by Total Assets is how the Leverage variable is calculated, and the Company Size variable is measured by the natural logarithm of Total Assets. The following is the equation of the research model:

\[
Y = a + \beta_1 X_1 + \beta_2 X_2 + \beta_3 X_3 + \beta_4 X_4 + \beta_5 X_5 + e
\]

Description:
- \(Y\) = Company's Financial Performance
- \(A\) = Constant Value
- \(\beta_1, \beta_2, \beta_3, \beta_4\) = Linear Regression Coefficient
- \(X_1\) = Total Asset Turnover
- \(X_2\) = Current Ratio
- \(X_3\) = Leverage
- \(X_4\) = Company Size
- \(E\) = Standard Error

### 3. METHODS

The variables independent used Total Asset Turnover, Current Ratio, Leverage, and Company Size. While the dependent variable is Company Financial Performance. All variables will be formulated in the table below.
Table 1 Variable Operationalization

<table>
<thead>
<tr>
<th>No.</th>
<th>Variable</th>
<th>Scale</th>
<th>Measurement</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Dependent Variable: Company's Financial Performance (Y)</td>
<td>Ratio</td>
<td>( \text{ROA} = \frac{\text{Net Income}}{\text{Total Assets}} )</td>
</tr>
<tr>
<td>2.</td>
<td>Independent Variable: Total Asset Turnover (X1)</td>
<td>Ratio</td>
<td>( \text{TATO} = \frac{\text{Sales}}{\text{Total Assets}} )</td>
</tr>
<tr>
<td>3.</td>
<td>Independent Variable: Current Ratio (X2)</td>
<td>Ratio</td>
<td>( \text{CR} = \frac{\text{Current Assets}}{\text{Current Liabilities}} )</td>
</tr>
<tr>
<td>4.</td>
<td>Independent Variable: Leverage (X3)</td>
<td>Ratio</td>
<td>( \text{DAR} = \frac{\text{Total Liabilities}}{\text{Total Assets}} )</td>
</tr>
<tr>
<td>5.</td>
<td>Independent Variable: Company Size (X4)</td>
<td>Ratio</td>
<td>( \text{CZ} = \ln(\text{Total Assets}) )</td>
</tr>
</tbody>
</table>

Table 2 The Result of Regression Test

Dependent Variable
Method: Panel Least Squares
Date: 10/18/21  Time: 03:42
Sample: 2017 2020
Periods included: 4
Cross-sections included: 26
Total panel (balanced) observations: 104

<table>
<thead>
<tr>
<th>Variable</th>
<th>Coefficient</th>
<th>Std. Error</th>
<th>t-Statistic</th>
<th>Prob.</th>
</tr>
</thead>
<tbody>
<tr>
<td>C</td>
<td>-1.155561</td>
<td>0.528960</td>
<td>-2.184590</td>
<td>0.0321</td>
</tr>
<tr>
<td>X1</td>
<td>0.088002</td>
<td>0.024498</td>
<td>3.592274</td>
<td>0.0006</td>
</tr>
<tr>
<td>X2</td>
<td>-0.010053</td>
<td>0.005155</td>
<td>-1.949991</td>
<td>0.0550</td>
</tr>
<tr>
<td>X3</td>
<td>-0.237786</td>
<td>0.057502</td>
<td>-4.135262</td>
<td>0.0001</td>
</tr>
<tr>
<td>X4</td>
<td>0.043771</td>
<td>0.017517</td>
<td>2.498767</td>
<td>0.0147</td>
</tr>
</tbody>
</table>

Effect Specification
Cross-section fixed (dummy variables)

- R-squared: 0.938910
- Adjusted R-squared: 0.914970
- S.E. of regression: 0.025281
- Sum squared resid: 0.047294
- Log-Quinn likelihood: 252.6102
- F-statistic: 39.21849
- Prob (F-statistic): 0.000000

- Mean dependent var: 0.102256
- S.D. dependent var: 0.086696
- Akaike info criterion: -4.280966
- Schwarz criterion: -3.518161
- Hannan-Quinn criterion: -3.971932
- Durbin-Watson stat: 2.064507

This test uses Jarque-Bera to see if the data being used is regularly distributed or not. In this test, 64 outliers were tested for data that needed to be removed, thus indicating that the current p-value of Jarque-Bera is 5.083940. This value shows results that are greater than the 5% significance value.
FINDINGS AND DISCUSSIONS

The goal of this research is to find out the relationship formed between the independent variables Total Asset Turnover (X₁), Current Ratio (X₂), Leverage (X₃), and Firm Size (X₄) on Financial Performance (Y). The level of confidence in these findings has been set at 95% and with a 5% level of statistical significance. The data included in the study has also passed the multicollinearity, heteroscedasticity, autocorrelation, and normality test. Based on the regression results using EViews version 12.0, Total Asset Turnover, Current Ratio, Leverage, and Company Size simultaneously have a significant positive effect on the Financial Performance. The financial performance is influenced by total asset turnover in a positive and significant way because the significance value of X₁ is less than the significant value set by the researcher, which is 5%. The Current Ratio has a negative effect and small impact on the Financial Performance of the company because the significant value of X₂ is greater than the significant value set by the researcher, which is 5%. Leverage has a negative effect and considerable impact on the firm financial performance because the significant value of X₃ is smaller than the significant value set by the researcher, which is 5%. Company size has a positive and significant effect on the Financial Performance of the Company because the significant value of X₄ is smaller than the significant value set by the researcher, which is 5%. The first hypothesis is accepted since TATO has a good impact on the financial success of the company. This test agrees with the tests conducted by M. Firza Alpi and Ade Gunawan (2018) [1]. Total asset turnover can determine operational decisions to be taken by management. When a company's asset turnover is higher, the company is considered good at maximizing its assets to generate sales. When sales are high, the company’s profit is similarly great.

The Current Ratio has a negative and small impact on the firm performance of a corporation so the second hypothesis is rejected. This test agrees with the test conducted by Agustin, Andi, and Vernetta (2021) [14] showing there is no influence on the Current Ratio on company performance. The negative direction signifies that the higher the Current Ratio, the lower the level of the company’s financial performance. This test also shows an insignificant effect on the company’s performance. The results that do not have an impact on this test are because there is a tendency for receivables in current assets which can cause the current ratio to have no impact on Return On Assets. After all, receivables can be said to be less liquid current assets. Companies that cannot meet their short-term obligations can pose a risk to their survival because operational needs cannot run smoothly. Leverage has a substantial bad effect on financial performance so the third hypothesis is accepted. This test agrees with that conducted by Aamir et al. (2021) [3] and Ilker (2021) [13]. High debt poses a bad risk to the financial performance of the company and reduces the ability to fulfill its responsibilities. However, if the debt level is good, the company becomes more efficient to generate profits because the additional capital can increase operations and investor confidence. Firm Size matters positively and significantly.
to the financial performance of the company to the fourth hypothesis is accepted. This test agrees with that conducted by Nasib (2019) [5]. Companies that have a large size will find it easier to get financial assistance because they are considered more reliable and able to repay the loan. When the company gets a large loan capital, the company can produce large quantities as well so that it can generate large profits and with the amount of capital owned by the company as a result of the large size of the company, management will also find it easier to develop the company by doing research and experiments to produce a new product to make a profit which leads to an improvement in the firm financial performance.

5. CONCLUSIONS

The goal of this research was to see if Total Asset Turnover, Current Ratio, Leverage, and Company Size had an impact on Company Financial Performance. Based on the findings of the analysis that has been carried out in this test which took samples from 2017 to 2020, consumer products manufacturing companies will be registered on the Indonesia Stock Exchange, it shows that the Total Asset Turnover, Current Ratio, Leverage, and Company Size not all of them have a bearing on the company's performance. There are 26 firms with 104 samples in total. This research utilizes the EViews 12.0 software to do a regression. From the test yield, it’s also possible to conclude that simultaneously all the independent in this study’s factors have a considerable beneficial impact on the financial performance, but it’s also possible to conclude that partially TATO has a meaningful effect and beneficial impact based on the financial results of a corporation, the Current Ratio has a negative and insignificant on the performance of corporate, Leverage hasn’t a positive and considerable impact on the financial firm performance, and company size has a good and strong impact.

The conclusions are expected to provide information for interested parties that not all variables can affect financial performance. Company performance can be influenced by several factors that need to be considered by parties such as investors, company management, etc. The limitations experienced in this study are (1) the size of the sample used in this study which was only used for four periods (2017 to 2020), (2) The study’s participants do not include all companies registered on the IDX, because this test only focuses on companies in the manufacturing industry, consumption industry sector and (3) The independent variables used in this research only consist of four variables, namely Total Asset Turnover, Current Ratio, Leverage, and Company Size so that it does not cover all variables that affect Company Financial Performance. The limitations of this research can be used as a lesson for further researchers to be able to increase the sample and increase the testing period, test other variables other than those already tested in this test, and future researchers should be permitted to use samples from sources other than manufacturers.

ACKNOWLEDGMENT

This work was supported by Universitas Tarumanagara, Jakarta, Indonesia.

REFERENCES


https://doi.org/10.24912/ijaeb.v1i1.375-382


