Profitability as a Mediator in the Effect of Firm Growth and Size on Firm Value: Evidence from Indonesia's Real Estate Subsector

Abstract

This study aims to examine the effect of firm growth and firm size on firm value, with profitability serving as a mediating variable. The research focuses on companies within the real estate sub-sector listed on the Indonesia Stock Exchange during the 2021–2023 period. A quantitative approach was employed using path analysis as the analytical method. The sample was selected through purposive sampling, resulting in 37 companies that met the research criteria. The empirical findings demonstrate that firm growth and firm size exert a significant positive influence on firm value, indicating that business expansion and larger firm scale contribute to higher market valuation. Furthermore, profitability is proven to mediate the relationship between both independent variables and firm value, thereby reinforcing its strategic role in translating internal corporate characteristics into improved market performance and economic value. These results contribute to the existing literature on value creation, particularly within the context of the Indonesian real estate industry.

Keywords: Profitibility, Firm Growth, Firm Size, and Firm Value.

A. INTRODUCTION

The capital market plays a strategic role in supporting national economic growth by providing long-term financing facilities for companies. In Indonesia, the real estate sub-sector has become one of the key segments within the property industry that has experienced rapid development. However, such growth has not always been accompanied by consistent increases in firm value. In fact, there are indications that several companies in the real estate sub-sector have experienced declining firm value, despite continuous increases in assets and business expansion.

Table. 1 Data on the Development of Price to Book Value in Real Estate Sub-Sector Companies for the period 2021-2024

Years	2022	2023	2024
Growth PBV	0,94%	0,22%	-0,41%

Source: Processed Data

This phenomenon is reflected in the Price to Book Value (PBV) ratios of real estate sub-sector companies listed on the Indonesia Stock Exchange (IDX) during the 2021–2024 period. As shown in Table 1, the average PBV has consistently declined year by year, indicating that despite growth in company size and assets, the market has not fully appreciated the firm value.The declining PBV implies that investors assign relatively low market value to the book value of companies. This condition may arise from imbalances between corporate growth and profitability, eventually affecting market perception of long-term prospects.

Firm value is a crucial indicator that reflects investors' perception of a company's success in creating long-term value and shareholder wealth. According to Harmono (2009), firm value is closely associated with shareholder prosperity and managerial performance. Ideally, an increase in firm growth and size should be followed by an increase in firm value. However, empirical findings indicate that this is not always the case. Revealed that high-growth companies may still suffer a decline in value if not supported by adequate profitability.

Profitability is one of the key internal factors influencing firm value, also assert that profitability plays a mediating role in aligning company growth strategies with long-term market valuation (Pratama & Wiksuana, 2016). Companies that prioritize aggressive expansion without considering operational efficiency tend to experience declining profitability, leading to lower firm value. Geralin and Purwanto (2022) emphasized that uncontrolled growth without efficiency may endanger a firm's financial performance. This aligns with the Pecking Order Theory by Myers and Majluf (1984), which posits that companies prefer internal financing to avoid asymmetric information costs from external sources. Excessive reliance on external financing, driven by weak profitability, may increase financial risk and ultimately reduce firm value.

Firm size is also frequently associated with operational stability and market power. Larger firms are presumed to have stronger bargaining power and easier access to capital. However, Kusumajaya (2011) found that firm size does not guarantee increased value if not accompanied by optimal profitability. Therefore, profitability may play a mediating role in explaining the relationship between firm characteristics and firm value.

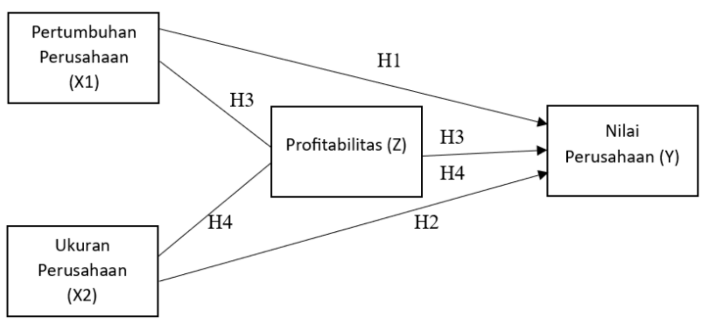
Several previous studies support this argument. Pristi and Anwar (2022) emphasized that profitability has a significant influence on firm value. Meanwhile, Putra and Badjra (2015) showed that high growth without adequate profitability tends to decrease market trust. Yulimtinan and Atiningsih (2021) stated that financial performance—especially profitability—strengthens the relationship between firm characteristics and investor assessment. Similarly, Suryandani (2018) found that firm growth only positively affects value when supported by sufficient earnings.

Recent findings by Takarini (2023) highlight that firm size, while influential, does not guarantee enhanced value unless operational efficiency and profitability are concurrently improved. Although many studies have examined the influence of firm growth and size on firm value, the empirical findings remain inconsistent, particularly regarding the mediating role of profitability. Some studies report strong relationships, while others find weak or insignificant results. This research gap serves as the foundation for the current study, which aims to analyze the effect of firm growth and firm size on firm value, with profitability as a mediating variable, in real estate sub-sector companies listed on the Indonesia Stock Exchange during the 2021–2024 period. This study is expected to provide empirical evidence on the critical role of profitability in increasing firm value amid aggressive business expansion.

B. LITERATURE REVIEW

Firm value represents the market's perception of a company's worth, and it is influenced by various internal factors such as firm growth, firm size, and profitability. According to Pecking Order Theory (Myers & Majluf, 1984), companies prioritize financing sources based on the level of asymmetric information, starting from internal funds, followed by debt, and lastly external equity. Firms with insufficient internal profitability tend to rely on external funding, which increases financial risk and potentially lowers firm value. In this context, firm growth and firm size may signal operational expansion and market strength, but these characteristics alone do not always guarantee value creation unless supported by sufficient profitability (Yulianti & Ramadhan, 2019; Kusumajaya, 2011) Rapid asset growth without strong earnings may cause inefficiency and erode investor confidence (Geralin & Purwanto, 2020). Thus, profitability serves as a mediating factor that links firm characteristics to firm value, especially in asset-intensive industries such as real estate. This review discusses the theoretical foundation and previous empirical studies regarding the influence of firm growth, firm size, and profitability on firm value.

Fig 1. Conceptual Framework



Firm Growth on Firm Value

Firm growth reflects the company's ability to expand its business operations and increase its assets. Growth is often perceived positively by investors, as it indicates the company’s potential to generate future returns. However, Yulianti and Ramadhan (2019) argued that growth alone is insufficient to increase firm value if it is not supported by profitability. Similarly, Geralin and Purwanto (2020) emphasized that uncontrolled growth without efficiency can threaten the company’s financial health and weaken investor confidence.

Firm Size on Firm Value

Firm size represents the scale and operational capacity of a company. Larger firms are typically perceived as more stable and capable of generating sustained earnings, which contributes positively to firm value. Firm size also reflects a company's resource availability and ability to access financing at favorable terms. However, large firm size does not always guarantee high value if it is not followed by effective asset utilization. Revealed that larger firms with poor profit margins may face stagnant or declining firm value, emphasizing that size must be supported by strong financial performance (Dewi and Abundanti, 2020).

Profitability on Firm Value

Profitability is a key determinant of firm value. High profitability signals good performance and effective management, which attracts investors and enhances firm value. Pristi and Anwar (2021) demonstrated that profitability significantly influences firm value. Likewise, Putra and Badjra (2021) found that declining profitability, even in growing firms, could reduce investor interest and firm valuation. Yulimtinan and Atiningsih (2021) also emphasized the role of financial performance in strengthening the relationship between firm characteristics and firm value.

Profitability as a Mediating Variable

Several studies have investigated the mediating role of profitability in the relationship between firm characteristics and firm value. Suryandani (2021) confirmed that firm growth impacts firm value more strongly when mediated by profitability. This suggests that profitability serves as a crucial mechanism through which internal company characteristics—such as size and growth—translate into improved firm valuation. In the context of the real estate sub-sector, which often experiences asset-heavy expansion, profitability becomes a key indicator of whether such growth is adding value or merely increasing operational risk. Emphasized that profitability mediates the impact of internal performance on investor perception, making it a vital pathway in enhancing firm value (Dewi & Ekadjaja, 2020)

C. RESEARCH METHODOLOGY

This This study adopts a quantitative research approach with an associative causal design to examine the direct and indirect relationships between firm growth, firm size, profitability, and firm value. The analysis focuses on the mediating role of profitability in the relationship between firm growth and firm size toward firm value. The population in this study consists of all real estate sub-sector companies listed on the Indonesia Stock Exchange (IDX) during the 2021–2024 period. Using purposive sampling, a total of 37 companies were selected as the research sample based on the criteria of data completeness and consistent listing throughout the research period. Secondary data were obtained from the annual financial statements of the selected companies. Data analysis was conducted using multiple linear regression to test direct effects, and the Sobel test to examine mediation. All statistical analyses, including classical assumption tests and significance tests (t-test, F-test, and R^2), were performed using SPSS software. The following table summarizes all the variables used in the research, the operational definition, and the measurement method:

Table 2. Operational Definition and Variable Measurement

Variable	Type	Operational Definition	Indicator / Measurement Formula	Source
Firm Value	Dependent (Y)	Firm value reflects market valuation and is measured using the Price to Book Value (PBV) ratio.	PBV= stock price / book value per share	Rizki & Takarini, 2021
Firm Growth	Independent (X1)	Firm growth refers to the increase in total company assets over time and is measured using the percentage change in total assets from the previous year.	PEG= (P/E Ratio) / Growth EPS	Bodie & Marcus, 2014
Firm Size	Independent (X2)	Firm size represents the scale of the company's resources and is measured by the natural logarithm of total assets.	Ln (Total Assets)	Putra & Badjra, 2015
Profitability	Mediating (Z)	The firm's capacity to Profitability Mediating (Z) generate profit from total assets..	ROA = Net Income / Total Assets	Putra & Badjra, 2021

D. RESULT AND DISCUSSION

Result

To conduct this research, we collected and calculated firm growth, firm size, profitability, and firm value during the period 2021–2024. The secondary data used in this study were obtained from the financial statements of real estate sub-sector companies listed on the Indonesia Stock Exchange (IDX) for the 2021–2024 period, as previously described.

Table 3. The Average Firm Growth, Firm Size, Profitability, and Firm Value

Tahun	Pertumbuhan Perusahaan (%)	Ukuran Perusahaan (satu satuan)	Profitabilitas (%)	Nilai Perusahaan (kali)
2021	-39,50	27,15	4,79	0,73
2022	-0,10	27,44	8,80	1,42
2023	2,10	28,13	-11,48	1,73
2024	-50,29	25,93	-241,78	1,02

Source: Data processed

Table 3 presents the annual average data of the four main variables in this study: During the 2021–2024 period, average firm growth experienced a significant downward trend. In 2021, growth stood at –39.50%, slightly improved to 2.10% in 2023, but then plunged sharply to –50.29% in 2024. This pattern indicates that companies in the real estate sub-sector faced operational challenges that hindered consistent year-on-year growth. Firm size remained relatively stable from 2021 to 2023, ranging from 27.15 to 28.13. However, it declined to 25.93 in 2024, suggesting a reduction in total assets or a downsizing of operational scale in several firms. Profitability showed a sharply negative trend. After peaking at 8.80% in 2022, it declined to –11.48% in 2023 and dropped drastically to –241.78% in 2024. This reflects significant financial losses experienced by many companies in the sub-sector. Firm value, as measured by the Price to Book Value (PBV) ratio, increased from 0.73 in 2021 to 1.74 in 2023, indicating improved market perception. However, it declined again to 1.02 in 2024, suggesting that the downturn in profitability and growth negatively impacted market valuation.

Table 4. Hypothesis Testing

No.	Relationship Between Variable	Path Coefficient	P-Value	Description
1.	Firm Growth (X1) -> Firm Value (Y)	0.178	0.010	Significant
2.	Firm Size (X2) -> Firm Value (Y)	0.568	0.001	Significant

Source: Data processed using SPSS

The results of hypothesis testing show that Firm Growth (X1) has a significant positive effect on Firm Value (Y), as indicated by a path coefficient of 0.087 and a p-value of 0.010. This finding supports the hypothesis that increased firm growth contributes directly to higher firm value. It suggests that expanding assets and business operations can improve market perceptions, reflecting positively on the company's valuation. Furthermore, Firm Size (X2) also exerts a significant positive influence on Firm Value (Y), with a path coefficient of 0.146 and a p-value of 0.001. This result confirms that larger firms, with greater resources and operational scale, tend to have higher firm value, likely due to increased investor confidence in the company's stability and market power. These results align with the Pecking Order Theory, emphasizing that internal characteristics such as growth and size can directly enhance firm value by signaling financial strength and long-term prospects to the market.

Table 5. Mediation Testing

No	Relationship Between Variable	Mediation Variable	Path Analysis	P-Value	Description
1	Firm Growth (X1) -> Firm Value (Y)	Profitability (Z)	0.053	0.0167	Significan
2	Firm Size (X2) -> Firm Value (Y)	Profitability (Z)	0.083	0.0069	Significan

Source: Data Processing

The results of the Mediation test, as shown in Table 5, demonstrate that Profitability significantly mediates the effect of Firm Growth on Firm Value, with a path coefficient of 0.053 and a p-value of 0.0167. This finding indicates that the positive influence of firm growth on firm value is partially transmitted through profitability. In other words, companies experiencing asset and business expansion tend to increase their firm value when such growth is supported by strong profitability performance. Similarly, Profitability also mediates the relationship between Firm Size and Firm Value, with a path coefficient of 0.083 and a p-value of 0.0069. This suggests that the larger the company, the greater the firm value it can achieve — provided that the company is able to maintain operational efficiency and generate stable profits. Without profitability, firm size alone may not necessarily translate into greater market valuation.

These results reinforce the strategic importance of profitability in linking internal firm characteristics — such as growth and size — to external market performance. The presence of significant mediation supports both the Pecking Order Theory, in which internally generated performance signals (like profitability) play a crucial role in enhancing firm value from an investor's perspective.

Discussion

The results of this study show that firm growth has a significant positive effect on firm value, with a path coefficient of 0.178 and a p-value of 0.010. This indicates that companies experiencing an increase in total assets or business expansion tend to have higher market valuations. Firm growth reflects the company's ability to seize opportunities and generate future cash flows, which increases investor confidence. These findings are in line with the Pecking Order Theory, which explains that firms prefer to use internal financing derived from retained earnings before seeking external funding. Investors often perceive growing companies as financially sound and self-reliant, leading to increased firm value.

In addition, the results demonstrate that firm size has a significant positive effect on firm value, with a path coefficient of 0.568 and a p-value of 0.001. Larger firms are generally considered to be more established and stable, with greater operational capacity, access to capital, and the ability to generate economies of scale. These characteristics make them more attractive in the eyes of investors, contributing to a higher valuation. This result supports the Signaling Theory, where firm size is seen as a credible signal of stability and long-term success.

Furthermore, the Sobel test results confirm that profitability mediates the relationship between firm growth and firm value, with an indirect effect of 0.053 and a p-value of 0.0167. This suggests that growth alone is not sufficient to increase firm value unless it is accompanied by strong profitability. Profitability enhances the effect of firm growth by showing that the growth is productive and financially beneficial. Similarly, profitability also mediates the effect of firm size on firm value, with an indirect effect of 0.083 and a p-value of 0.0069. This indicates that large firms are more likely to be valued highly when they are able to generate consistent profits. Without profitability, firm size alone may not guarantee investor confidence.

These findings highlight the important role of profitability in converting internal company characteristics—such as growth and size—into higher firm value. The existence of significant mediation supports the theoretical perspective of both the Pecking Order Theory. Profitability serves as a signal of the company's financial health and performance, reinforcing investor trust and enhancing firm value in the real estate subsector.

E. CONCLUSION

The results of this study conclude that firm growth has a significant positive effect on firm value, indicating that companies with higher growth levels tend to have better market valuations. Firm size also shows a significant positive effect on firm value, suggesting that larger firms are more likely to be valued higher due to their greater resources and operational advantages. In addition, profitability is proven to significantly mediate the relationship between both firm growth and firm size on firm value. This means that growth and size contribute more effectively to increasing firm value when accompanied by strong profitability. Overall, these findings emphasize the important role of profitability in strengthening the influence of internal company factors on firm value within the real estate sector.

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