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Analysis of the Influence of Financial Leverage on Financial Performance at Mining, Oil and Gas Companies Listed on Indonesia Stock Exchange

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Abstract. This paper aims to determine the effect of the use of debt to finance the company's operations on the performance of companies in the industry mining, oil and gas. The model used in this research is quantitative research. The samples used were 151 samples. This sample consists of companies mining, oil and gas listed on the Indonesian Stock Exchange from 2010-2014. Data analysis method used is using simple regression analysis. Research by a simple regression method with earnings per shares, net profit margin and return on equity as the dependent variable and the debt to equity ratio as independent variables. Results of this study indicate that the use of debt or debt to equity ratio does not significantly affect the company's financial performance such as earnings per shares, net profit margin and return on equity. The use of high debt to meet the company's operations are not necessarily able to improve financial performance.

Keywords: financial leverage, financial performance

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Introduction

The business entity in carrying out its operational activities is much financing with debt. The use of this debt is called financial leverage. Financial leverage is the way companies finance their activities. Company operational activities can be financed by financial leverage as an effort to sustain the company's business.

The majority of companies still use financial leverage despite the risks posed large enough. The risk is a reduction in net profit for shareholders, especially for ordinary shareholders. Companies still choose to use financial leverage, because if the entrepreneur invests a small portion of all funds required by the company then the risk will be borne by the creditor. Companies can make a profit on the use of the debt, and return on equity (ROE) may increase. Financial leverage is the use of a source of funds with a fixed expense in the hope that it will provide a greater profit than its fixed expense so as to increase the benefits available to shareholders. Rehman (2013) shows different results i.e. high debt will increase the ROE with the condition of the company is not good, on the contrary when the condition of the company is good then the increase in debt will cause the decline in ROE.

Financial leverage also has an effect on earnings per share, high financial leverage can add investment funds. The company expects to increase EPS with the additional investment fund. Financial leverage is the use of funds with a fixed expense that is in the hope to enlarge earnings per share. Rehman (2013) shows the result that there is a negative relationship between debts (DER) on EPS. Debts increase then interest payments will increase, but EPS will decrease.

Research Akhtar et al., (2012) states that financial leverage has a positive relationship with financial performance. Financial leverage does not always have a positive relationship or influence on financial performance, so similar research needs to be done to know exactly how the relationship or influence. Research Pachori & Totala (2012) has different results, in his research states that there is no significant influence of financial leverage on shareholder returns and market capitalization. Shareholder returns and market capitalization are part of the financial performance.

Multinational companies have more role for economic development in a country especially in Indonesia. These companies tend to use large capital in the implementation of the company's operations. The capital usually uses a loan or debt from another party, the loan is called financial leverage. One of the multinational companies is mostly from the mining, petroleum and gas sectors. The mining, petroleum and gas sectors are the most fertile operating ground for multinational companies.

This research will examine the influence of the use of financial leverage to financial performance in the mining, petroleum and gas sector companies listed on the Indonesia Stock Exchange. Mining, petroleum and gas companies are unique in terms of the use of financial leverage in running operations. The company tends to use a huge loan or debt to support its operational costs.

Research Rehman (2013) examines the financial leverage of financial performance in the food industry sector, especially sugar in Pakistan. Research Akhtar et al., (2012) examines the financial leverage of financial performance in energy sector companies in Pakistan. The study Rehman (2013) obtained negative results on the financial performance of profit per share, ratio of return on capital and net profit margin. The results of the study Rehman (2013) are not in line with the results of the study Akhtar *et al.,* (2012) which show positive results on the financial performance of profit per share sheet, return of capital and net profit margin. This study would like to examine the mining, petroleum and gas companies in Indonesia whether in accordance with the study Rehman (2013) or Akhtar *et al.,* (2012). The differences in this study with the previous sectors selected by researchers are the mining, petroleum and gas sectors, while research Rehman (2013) in the food sector and Akhtar *et al.,* (2012) in the energy industry sector. This study uses only three components in the financial performance of profit per share sheet, return ratio and net profit margin. The three components are due to different results from the studies Rehman (2013) and Akhtar *et al.,* (2012). If the research is in line with the results of the study Akhtar *et al.,* (2012), the use of financial leverage for the operations of mining, petroleum and gas companies in Indonesia is the right policy for the company.

Based on the explanation in the introduction, the problem in this research is whether financial leverage has an effect on financial performance which includes Return on Equity (ROE), Earning per Share (EPS), and Net Profit Margin (NPM).

The purpose of this study is to examine the influence between financial leverage and financial performance in mining companies, oil and gas listed on the Indonesia Stock Exchange. This study is more

specialized to examine the components of financial performance.

Literature Review

Trade off Theory

Trade off theory (TOT) can estimate debt levels that should increase along with asset size, maturity, tangible assets, profits and effective tax rates. Trade off theory (TOT) can also estimate debt levels may decrease along with intangible assets, risks, and deferred taxes (Singh *et al.,* 2008). Trade off theory (TOT) is expressed as a company that has an optimal debt level in its capital structure, due to the profit and cost of the debt (Wardianto, 2012).

Financial Performance

The experts define the financial performance of the company as an analysis conducted to see how far a company has implemented with the rules of financial implementation properly and correctly (Fahmi, 2013). The measuring instrument used to measure financial performance is usually used in the form of ratio analysis.

The analysis of financial ratios is an analysis by comparing one post with the other financial statements individually or jointly in order to know the relationship between certain items either in the balance sheet or in profit and loss (Jumingan, 2011). Some of analyzes normally used in analyzing financial performance include the following:

a. Earnings per Share (EPS)

Earnings per share or Earnings per Share (EPS) is the amount of net profit per share that a company can achieve when operating. Earnings per Share as a ratio that shows the share of earnings for each share obtained by investors (Darmadji & Fakhruddin, 2006). Earnings per Share is the ratio between income after tax with the number of shares outstanding (Widiatmojo, 2005).

b. Net Profit Margin (NPM)

Net Profit Margin (NPM) is basically one of the ratios used to demonstrate a company's ability to generate net income. Net profit margin is the ratio between net income and sales (Bastian & Suhardjono, 2006). This ratio is one of the important ratios for operational managers, because this ratio is able to reflect the sales pricing strategy that the company will apply. This ratio is also able to control the operating expenses.

c. Return on Equity (ROE)

Return on Equity (ROE) used in the research is to measure the net income earned by the owner of the company on the invested own capital. ROE measures a company's ability to make a profit available to its shareholders.

Financial Leverage

Financial leverage as a potential use of fixed financial costs to increase the effect of changes in earnings before interest and taxes on EPS. Financial leverage arises from the utilization of sources of funds caused by debt, so the company must bear the debt and burdened by the cost of interest. Leverage ratio is the ratio used to measure the extent to which the company's assets are financed with debt.

The greater use of financial leverage brings a positive impact if the revenue received from the use of such funds is greater than the financial burden spent (Ritonga *et al.,* 2014). This indicates that if the income received is less than the financial burden then it is a negative impact of the use of financial leverage. Based on the above description can be concluded some hypothesis include:

H1: Debt to equity ratio positively affects earning per shares

H2: Debt to equity ratio positively affects net profit margin

H3: Debt to equity ratio positively affects return on equity

Research Methods

The object of this research is mining, petroleum and gas company listed in Indonesia Stock Exchange (IDX), by collecting financial report year 2010-2014. This data is obtained from the official website BEI www.idx.go.id by way of downloading the financial statements.

The sampling technique used in this study is purposive sampling with the criteria or consideration in the sampling is a manufacturing company listed on the BEI from 2010-2014 period. The manufacturing company is only a company engaged in mining, petroleum and gas. These companies publish financial statements from 2010-2014.

Results and Discussion

Characteristics of Respondents

In Table 1 shows the total number of listed companies on the IDX as of December 31, 2014 as many as 506 companies. Non-mining, petroleum and gas sector companies accounted for 465 while for mining, oil and gas sector 41 companies. The entire mining, petroleum and gas sectors have been samples of this study. Data was selected using cross-sectional method.

Table 1
Companies listed BEI

Companies listed BEI	Number
Non Mining, Oil and Gas	465
Mining, Oil and Gas	41
Total	506

Source: IDX data 2014

Hypothesis Test Results

Regression analysis is used to see the effect of independent variables on dependent variable and predict the value of dependent variable by using independent variable. The regression equation in this research is as follows:

$$EPS = a + b_1(DER) + e \quad (1)$$
$$NPM = a + b_1(DER) + e \quad (2)$$
$$ROE = a + b_1(DER) + e \quad (3)$$

EPS = Earning per Shares
NPM = Net Profit Marjin
ROE = Return on Equity
DER = Debt to Equity Ratio
A = Coefficient of constants
B = Constants change of variable X to Y
E = error

Table 2
Simple Linear Regression Test Result

	Model 1		
	B	R2	Sig.
DER → EPS	0.207	0.011	0.198
	Model 2		
	B	R2	Sig.
DER → NPM	-0.077	0.001	0.697
	Model 3		
	B	R2	Sig.
DER → ROE	-0.262	0.015	0.128

Source: Results of SPSS 16.0

Discussion

Based on Table 2 it can be seen that the significant value of each hypothesis testing has a value of 0.198, 0.697 and 0.128. These results indicate that significant values> 0.05 so that H1, H2, and H3 are not supported.

Conclusion

The results of this study indicate that the debt to equity ratio (DER) has no significant effect on the three components of financial performance, namely earnings per share (EPS), net profit margin (NPM) and return on equity (ROE) in the mining, petroleum and gas that is done in Indonesia. Means the use of debt in running the operations of mining companies, petroleum and gas can not improve the financial performance of the company.

The use of debt to run the company's operations must be managed properly, if the management of debt funds are not managed properly it will impact the company's profit. Increasing the burden or cost due to the debt will reduce the company's profit. A decrease in corporate earnings will result in a decrease in EPS, NPM and ROE relating to corporate earnings. Assessment whether or not a company can be seen from whether or not the three components of the financial performance.

This research is replication of previous research, so furthermore it is expected that the development in research variables so that the scope of the results of this study more widely. Development or addition of these variables aims to maximize the results of research that can be accounted for and applied in the company.

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