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# Financial Performance Leverage to Drive Profit Growth in Manufacturing Companies

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***Abstract:*** *The company's profit growth is a key factor in assessing the company's performance. Profit growth refers to the increase or positive change of profits generated by a company over time. Then leverage, which is the ratio of debt to equity, is one of the factors that can affect a company's profit growth. This study aims to analyze the effect of leverage on profit growth in the object of manufacturing companies. The method used in this study is regression analysis. The results showed that the DAR and DER ratios fluctuated, but for the whole during the study period both ratios were still at healthy levels. An insignificant relationship between leverage and profit growth of manufacturing companies. Leverage with debt to asset ratio (DAR) and debt to equity ratio (DER) has no influence on the company's profit growth. Then the value of R square indicates a relationship that is not significant but positive. The research provides findings in an understanding of how leverage does not necessarily affect a company's profit growth.*

***Keywords:*** *Financial Performance, Leverage, Profit Growth, Profits, Finance*

## I. Introduction

A manufacturing company is a type of business that implements production processes to produce finished goods that can be sold to consumers. These companies usually have production facilities, such as factories or workshops, where raw materials are transformed into the final product through various stages of production (Felsberger et al., 2022). Examples of manufacturing companies include automobile factories, electronics factories, textile factories, and so on. Companies play a significant role in the economy by creating jobs and contributing to economic growth (Istan, 2021).

The COVID-19 pandemic has had a significant impact on industries around the world (Utama & Mustika, 2022). Changes that occurred in the manufacturing industry during and after the COVID-19 pandemic included reduced production, lockdowns and travel restrictions making it difficult for companies to run full operations. Many manufacturing companies are struggling due to disruptions to global supply chains (Corbet et al., 2022). In the wake of the pandemic, some companies are considering moving or diversifying their supply chains to be more resilient to similar risks in the future. This includes moving production to other countries or increasing local production. The COVID-19 pandemic has changed hygiene and safety standards in manufacturing work environments. Strict sanitation protocols and individual protections such as mask use and social distancing have been implemented to protect employees. During the pandemic, the demand for certain products has decreased drastically while the demand for other products has increased. Some manufacturing companies are switching to producing products that are more relevant to COVID-19 needs, such as personal protective equipment (PPE), medical equipment, and sanitary products. After the pandemic, changes in the manufacturing industry that occurred during the pandemic are expected to affect their production processes and business strategies. Manufacturing companies tend to be more cautious in managing risk and diversifying their supply chains, while still adopting new technologies to improve operational efficiency (Ponsam et al., 2021).

Manufacturing companies carry out comprehensive production planning, including raw material requirements planning, capacity planning, and production process planning (Maisiri & Van Dyk, 2021). It aims to ensure production efficiency and avoid shortages or excess inventory. Manufacturing companies must ensure sufficient supply of raw materials to meet production needs. The raw material procurement process includes supplier selection, price negotiation, delivery, and quality control. The production process in a manufacturing enterprise involves various stages, such as component assembly, material processing, and final product forming.

Manufacturing companies must maintain the quality of the products produced by conducting testing and quality control at every stage of production (Obradović et al., 2021). This control can be carried out using special testing tools, quality standards and product inspections. After the product is completed, the manufacturing company carries out a packaging process to protect the product and facilitate distribution. Then, the product is distributed to consumers through specified distribution channels. Manufacturing companies are also responsible for carrying out maintenance and maintenance of production machinery and equipment. Manufacturing companies conduct continuous research and development to improve products, production processes, and efficiency.

The profit growth of manufacturing companies is a key factor in assessing the company's performance (Lesmana et al., 2022). Profit growth refers to the increase or positive change of profits generated by a company over time (Swathi, 2022). Profit growth is often used as an important indicator of financial performance because it reflects a company's ability to generate higher profits over a period of time (Utama, A. N. B., 2023). Profit growth in manufacturing companies can be influenced by various factors, such as increased sales (Maryati & Siswanti, 2022), Cost efficiency, improved profit margins, and good capital management, especially in managing corporate debt (Utama et al., 2020).

Leverage, which is the ratio of debt to equity, is one of the factors that can affect a company's profit growth (Hakim et al., 2020). The relationship between a company's profit growth and profit growth can vary depending on several factors. Some things to consider in this context include the use of debt can help companies expand their operations, make investments, and generate higher profit growth (Beck & Garris, 2019). Debt earned at interest rates lower than the expected rate of return on investments can increase the company's profit growth (Frazzini & Pedersen, 2022). Debt also carries the risk of interest that must be paid by the company (Istiak & Serletis, 2020). If interest costs are too high, it can affect the company's profits and hinder significant profit growth (Hermansson & Jonsson, 2021). High levels of leverage also carry financial risks. If a company's revenue declines or experiences financial difficulties, debt management becomes more difficult and can hinder profit growth (Utama, A. N. B., & Syarif, A. 2023).

This study aims to analyze the effect of leverage in driving profit growth in manufacturing companies. In this study, researchers took samples from one of the largest manufacturing companies in Indonesia, namely PT. Indofood Sukses Makmur, Tbk. The company is listed on the Indonesia Stock Exchange and was established in 1990. PT. Indofood Sukses Makmur Tbk has various famous brands such as Indomie, Indomilk, Pop Mie, and many more. They operate in a variety of business segments including instant food and beverages, soft drinks, food packaging, agribusiness, and distribution. PT Indofood Sukses Makmur Tbk continues to grow and become one of the market leaders in the Indonesian food and beverage industry. Based on the explanation above, the main problem to be discussed is how to describe the development of leverage ratios and profit growth? How does leverage drive partial profit growth? then simultaneous? and how much influence does leverage have on the company's profit growth?

## II. Research Methods

This research uses a quantitative model with the object of research is one of the largest manufacturing companies in Indonesia, namely PT. Indofood Sukses Makmur, Tbk. The data used in this analysis is secondary data obtained from the company's annual financial statements during the period 2018 to 2022. The independent variables in this study are leverage variables, namely Debt to Assets Ratio (DAR) and Debt to Equity Ratio (DER). Both of these indicators are used to measure the extent to which a company uses debt in its financial structure. The Debt-to-Assets Ratio (DAR) calculates the percentage of a company's total assets that are financed with debt. The formula DAR is as follows:
DAR = Total Debt / Total Assets

DAR helps in assessing the level of financial risk of the company and how much debt liability the company has in relation to its assets. The higher the DAR, the greater the share of the company's assets financed with debt. Then the debt-to-equity ratio (DER), DER measures the extent to which the company uses owner's capital compared to debt. The formula DER is as follows:

DER = Total Debt / Equity

DER provides an overview of financing a company with debt compared to financing with owner's capital. The higher the DER, the greater the share of the company's capital financed with debt.

This study used regression analysis method (Sugiyono, 2020) to examine the relationship between leverage and profit growth of manufacturing companies. Data analysis and processed data collected using excel software in Microsoft Office 365. The initial step of the researcher is to process data on debt, total assets, capital, and profit growth from financial statements. Then, to find out how the influence of leverage in driving partial profit growth using the t test, then the simultaneous influence using the f test, and find out the magnitude of the influence of leverage on the company's profit growth using the R square. R square is a number whose magnitude is between 0 and 1 which indicates the magnitude of the combination of independent variables affecting the value of the dependent variable. The value of R square is used to determine how much influence a particular independent variable has on the dependent variable (Daniar Pramita et al., 2021).

## III. Results And Discussion

The processed data of researchers from the financial statements of PT. Indofood Sukses Makmur Tbk obtained an overview of debt to asset ratio, debt to equity ratio and profit growth, as follows:

Table 3.1. Development of Debt to Asset Ratio (DAR), (Debt to Equity Ratio) DER and Profit Growth PT. Indofood Sukses Makmur Tbk Period 2018 s.d. 2022

| Year | DAR | DER | Profit Growth (in millions of rupiah) |
|---|---|---|---|
| 2018 | 0,48 | 0,93 | 6.350.788 |
| 2019 | 0,44 | 0,77 | 6.588.662 |
| 2020 | 0,51 | 1,06 | 9.241.113 |
| 2021 | 0,51 | 1,06 | 11.965.911 |
| 2022 | 0,48 | 0,93 | 10.853.116 |
| Jumlah | 2,43 | 4,76 | 44.999.590 |
| Rata-rata | 0,49 | 0,95 | 8.999.918 |

Source: Annual Report PT. Indofood Sukses Makmur Tbk, Data processed 2023

Based on the table above, it can be seen that the DAR and DER ratio figures fluctuate, but for whole during the period 2018 to 2022, both ratios are still at a healthy number of the company's debt ratio because they are located at a number smaller than 2. Profit growth also showed a good number because it continued to rise, but total profit in 2022 regressed when compared to total profit in 2021.

Then a t test was carried out to determine the effect of leverage (DAR and DER) partially on profit growth with the following results:

Table 3.2. Coefficient Independent Variable

| | *Coefficients* | *Standard Error* | *t Stat* | *P-value* |
|---|---|---|---|---|
| Intercept | 7718247,448 | 196216808,4 | 0,039335 | 0,972196 |
| DAR | -52239110,58 | 859430508,5 | -0,06078 | 0,957059 |
| DER | 28027466,25 | 233350917,9 | 0,120109 | 0,915375 |

Source: Output excel microsoft office 365

Based on table 3.2. It can be seen that the significance figure on the DAR is 0.95709, this shows that the DAR ratio does not significantly affect profit growth because the significance > 0.05. Then the significance figure on DER is 0.915375, this also shows that the DER ratio does not significantly affect profit growth because the significance > 0.05.

The next step is to simultaneously test the effect of leverage on profit growth, using the Microsoft Office 365 excel application as follows:

Table 3.3. Anova

| | *df* | *SS* | *MS* | *F* | *Significance F* |
|---|---|---|---|---|---|
| Regression | 2 | 10817437763447,6 | 5408718881723,78 | 0,75624 | 0,569398273 |
| Residual | 2 | 14304239822266,4 | 7152119911133,22 | | |
| Total | 4 | 25121677585714 | | | |

Source: Output excel microsoft office 365

Based on table 3.3. It can be seen that the simultaneous significance figure of 0.569398273, this shows that together DAR and DER do not significantly affect profit growth even though both ratios show good ratio figures for the company.

Then to find out the relationship between leverage and profit growth, the following data is obtained:

Table 3.4. Summary Output

| *Regression Statistics* | |
|---|---|
| Multiple R | 0,6562025 |
| R Square | 0,4306017 |
| Adjusted R Square | -0,1387965 |
| Standard Error | 2674344,8 |
| Observations | 5 |

Sumber: Output excel microsoft office 365

The relationship of leverage to company profit growth using R square shows a number of 0.4306017 which indicates the magnitude of the combination of independent variables affects the value of the dependent variable. The value of the R square indicates a relationship that is not significant but positive. The findings of this study show that there is no significant relationship between leverage and profit growth of manufacturing companies. Leverage does not have a significant effect on the company's profit growth. That is, the higher the level of leverage of a company, the company's profit growth does not necessarily increase and vice versa.

## IV. Conclusion

Based on the results of the study, it can be concluded that the ratio of DAR and DER during the period 2018 to 2022 is still at a healthy number of the company's debt ratio because it is located at a number smaller than 2. Profit growth also shows a good number because it continues to rise, but total profit in 2022 has regressed when compared to total profit in 2021. Leverage in this study using the ratio of DAR and DER does not have a significant effect on the profit growth of manufacturing companies either partially or simultaneously. The relationship of leverage to company profit growth using R square shows a number of 0.4306017 which indicates the magnitude of the combination of independent variables affects the value of the dependent variable. The value of the R square indicates a relationship that is not significant but positive.

Companies can still use leverage with various other variables as a strategy to increase profit growth, but, keep in mind that unwise use of leverage can bring financial risks to the company. Therefore, company management must pay close attention to the use of leverage in an effort to increase profit growth or company value.

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