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Leverage and GCG Effects on Financial Performance Moderated by Firm Size

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Abstract

This research aims to empirically analyze the influence of leverage and Good Corporate Governance (GCG) on financial performance, with firm size functioning as a moderating variable, specifically within the hospitality industry in a Regency. The hospitality sector is a crucial part of the service industry that needs to be developed to foster new opportunities and enhance performance through competitive advantages. Employing a mixed methods approach, the study utilized purposive sampling to select a total of 117 industry units. Data analysis was conducted using the Moderated Regression Analysis (MRA) method. The results reveal that firm size does not moderate the effect of leverage on financial performance. Nonetheless, the GCG components namely the size of the board of directors, board of commissioners, and institutional ownership demonstrate a significant impact on financial performance when firm size is used as a moderating factor. Based on these findings, it can be concluded that effective implementation of GCG elements, supported by firm size, can strengthen financial performance in the hospitality industry. However, firm size alone is insufficient to influence the relationship between leverage and performance in this sector.

Keywords

Financial Performance, Firm Size, Good Corporate Governance, Hospitality Industry, Leverage.

1. Introduction

In the face of increasingly intense business competition, companies are expected to continuously enhance their performance and expand their operations to attain superior competitiveness. Financial performance serves as a key metric in assessing a company's success in managing its business activities (Meiyana & Aisyah, 2019). Moreover, financial performance illustrates a company's future potential and functions as an important tool for evaluating and sustaining its long-term viability (Kirana & Wahyudi, 2016). It is also one of the critical factors' investors consider when making investment decisions (Mandal & Al-ahdal, 2018).

The Borobudur area, which is located in Magelang Regency, has been designated as a National Tourism Strategic Area (*Kawasan Strategis Pariwisata Nasional/ KSPN*) for 2010-2025. The surge in tourists has had a positive impact on the hospitality industry in Magelang Regency (Verawati et al., 2023). However, according to data obtained by researchers, the average performance of the hospitality industry in Magelang Regency is 2.78%. This value is still below the industry standard average, namely 5.98%. The hospitality industry is an important service segment that needs to be developed to generate opportunities and increase performance through competitive advantage. Some of the hospitality industries in Magelang Regency that need attention to support tourism development in the Borobudur area are hotels, homestays, and Village Economic Centers (*Balai Ekonomi Desa/ Balkondes*).

Leverage functions as a key instrument for evaluating a company's ability to fulfill its financial commitments, both in the short and long term (Wati et al., 2024). It holds a strong correlation with financial performance, as it illustrates the degree to which a company relies on debt to improve its financial results (Mandal & Al-ahdal, 2018). In this research, leverage is assessed using the Debt-to-Equity Ratio (DER), which measures a firm's capacity to meet long-term obligations through its equity (Antikasari et al., 2020). Empirical studies by Widyari et al. (2022) and Verawat et al. (2023) support the notion that leverage affects financial performance. Nonetheless, a differing perspective from Lukviarman (2016) indicates that leverage has no significant effect on financial performance when the factor of firm size is considered.

Good Corporate Governance (GCG) refers to a governance framework that directs and oversees corporate operations, aiming to enhance company performance and ensure sustainability (Lukviarman, 2016; Nurhana et al., 2021). As stated Ambarwati et al. (2022), GCG is a management concept designed to improve managerial effectiveness and uphold accountability to stakeholders within a structured regulatory environment. In this study, GCG is assessed through three indicators: The composition of the board of commissioners, the existence of an audit committee, and the level of institutional ownership are key components. According to Khasanah and Sucipto (2020), GCG significantly influences financial performance. However, contrasting results are presented in Antikasari et al. (2020), which shows that when firm size is introduced as a moderating variable, GCG no longer has a significant impact on financial performance.

Based on the gap in phenomena and inconsistencies in the results of previous research which have been described previously, this is the reason behind this research. If business performance in the hospitality industry in Magelang Regency can be improved, it can encourage the development of the Borobudur Area as a KSPN in 2010-2025. By using a mix-method, this research provides comprehensive findings in the form of quantitative data and perceptions of hospitality industry players. Second, this research provides new evidence because this research focuses on leverage, GCG, and company size as variables to strengthen or weaken the relationship between variables whose main focus is the hospitality sector in Magelang Regency. Therefore, this study aims to examine the effect of leverage and

GCG on the financial performance of hospitality businesses in Magelang Regency, with firm size as a moderating variable.

2. Literature Review and Hypothesis Development

2.1. Agency Theory

Agency theory, first proposed by Jensen and Meckling (1976) explains the dynamic between a principal and an agent, in which the principal delegates decision-making authority to the agent. This theory suggests that the separation of control between owners and managers can lead to conflicts of interest, commonly referred to as agency problems Ningsih and Wuryani, (2021). These conflicts stem from divergent goals and result in information asymmetry, which in turn generates agency costs. The application of GCG serves as a mechanism to guide and oversee company operations, thereby minimizing agency costs (Himawan & Fazriah, 2021; Andiny & Hartono, 2022). Agency theory underpins the assumption that improved corporate performance can be realized through the effective implementation of GCG practices (Lukviarman, 2016). In this study, the linkage of agency theory highlights that sound financial outcomes are achievable through the adoption of prudent corporate governance strategies.

Pecking order theory argues that a company will determine funding decisions by following a hierarchy of funding sources preferred by the company. Companies prefer to choose funding from internal financing because it is considered to have a lower risk when compared to other funding sources (Purwanti, 2021). Companies prefer to choose internal financing because it has low risk. This theory assumes that companies that choose internal funding sources or small debt will provide high profits, thereby improving the company's financial performance (Antikasari et al., 2020).

2.2. Leverage, Governance, and Ownership on Financial Performance

Leverage is a key indicator of a company's capacity to meet financial obligations in the short and long term, and is crucial for enhancing financial outcomes (Kirana & Wahyudi, 2016). This study uses the DER to measure leverage, indicating the proportion of total liabilities to equity (Ghozali, 2018). Based on pecking order theory, minimizing external debt can improve profitability and financial performance. A lower leverage ratio signals stronger financial health. Empirical findings by Widyari et al. (2022) and Ningsih and Wuryani (2021) also confirm that leverage significantly affects financial performance. The board of commissioners plays a key role in corporate governance by mediating between shareholders and management (Ambarwati et al., 2022; Gemilang & Wiyono, 2022). Based on agency theory, stronger governance supported by a larger board can reduce information asymmetry and enhance financial performance. Empirical studies by Andika and Wijayanti (2017) and Wulandari and Tan (2023) confirm the board's significant impact on firm performance.

The audit committee is vital in enhancing the board of commissioners' oversight of financial reporting, risk management, auditing, and governance practices (Shanti, 2020). In agency theory, it helps reduce stakeholder conflicts through supervision Widyari et al. (2022) which can improve financial performance. A larger audit committee often ensures stronger oversight of financial disclosures, leading to better outcomes. Empirical studies by Purwanti (2021) confirm its significant impact on firm performance. Institutional ownership strengthens corporate supervision by monitoring managerial actions and reducing conflicts of interest between management and shareholders, as outlined in agency theory (Kusdiyanto & Kusumaningrum, 2016; Andika & Wijayanti, 2017). A higher proportion of institutional ownership implies stronger oversight, which is expected to enhance

financial performance. Additionally, firms with larger assets tend to achieve higher profits.

H1: Leverage has a significant effect on financial performance.

H2: Board of commissioners has a significant effect on financial performance.

H3: Audit committee has a significant effect on financial performance.

H4: Institutional ownership has a significant effect on financial performance.

2.3. Leverage on financial performance through company size

Companies with large asset bases are typically in a stronger position to meet their financial commitments. The scale of a firm's assets plays a crucial role in determining its future financial performance (Yusuf et al., 2022). Drawing from the pecking order theory, businesses that emphasize the use of internal financing and demonstrate effective and efficient asset management are more likely to achieve higher profitability, thereby improving their overall financial outcomes (Antikasari et al., 2020). Empirical evidence from Arummingsih (2018) and Ibhagui and Olokoyo (2018) suggests that leverage has an impact on financial performance, and that firm size serves as a moderating variable in this relationship. These insights imply that the size of a firm can influence the degree to which leverage affects financial performance.

Agency theory posits that conflicts may arise due to differing interests between principals and agents. To reduce such conflicts, these divergent interests must be aligned. The board of commissioners plays a crucial role in fostering an objective governance environment that aligns the company's goals with those of its stakeholders (Himawan & Fazriah, 2021; Putri & Mulyati, 2024). This alignment is expected to lead to more effective asset management, thereby enhancing the company's financial performance.

H5: Leverage has a significant effect on financial performance through company size.

H6: Board of commissioners has a significant effect on financial performance through company size.

2.4. Institutional Ownership, Audit Committee, and Firm Performance

Based on agency theory, there are differences in the division of roles between owners and management which can give rise to conflicts between principals and agents (Wahyuni & Erawati, 2019). This difference gives rise to information asymmetry which has an impact on the emergence of agency costs. Audit committees in public company entities have a positive impact in reducing agency costs (Himawan & Fazriah, 2021). High company size represents high company assets. Effective asset management can provide incentives for companies to improve financial performance. In the long term, large assets and effective management will increase profits and are believed to be able to cover agency costs. The results of research conducted Amelia et al. (2023) show that the audit committee influences financial performance, with the moderating variable being company size.

As stated by Jensen and Meckling (1976) institutional ownership plays a significant role in reducing agency conflicts between shareholders and management. Drawing on agency theory, such conflicts emerge due to diverging interests between principals and agents. Institutional ownership contributes to mitigating these conflicts by facilitating more effective oversight. Meanwhile, Himawan and Fazriah (2021) suggests that larger firms possess stronger financial capabilities to enhance performance, however, they may also encounter more complex agency problems.

H7: Audit committees has a significant effect on financial performance through company size.

H8: Institutional ownership has a significant effect on financial performance through company size.

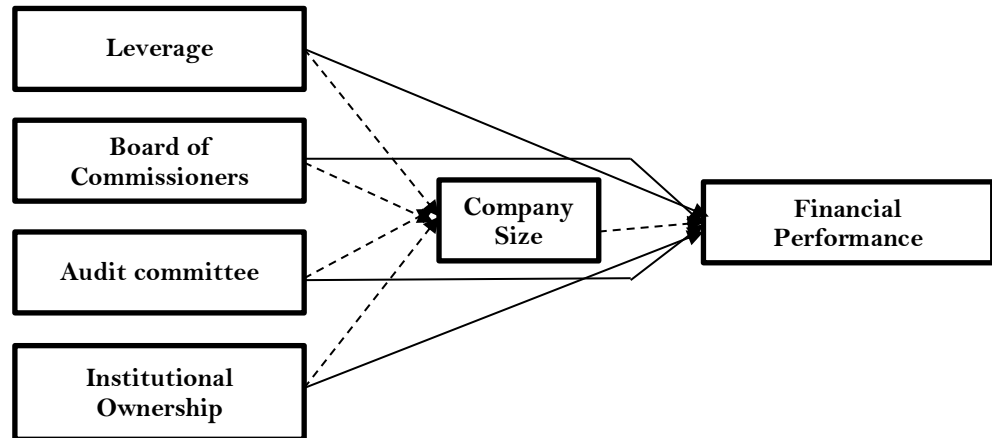


Figure 1. Conceptual Framework

Figure 1 shows a research framework that illustrates the relationship between several independent variables, intervening variables, and dependent variables. The independent variables consist of leverage, board of commissioners, audit committee, and institutional ownership, each of which is assumed to have an influence on the company's Financial Performance as the dependent variable (Sularto & Gantino, 2023). Among these relationships, there is Company Size which acts as an intervening or mediating variable, which can strengthen or weaken the influence of independent variables on financial performance. This framework shows an attempt to analyze how corporate governance structure and internal financial factors contribute to financial performance by considering the role of company size as an intermediary factor.

3. Methods

This research is a type the analytical uses mixed methods, namely quantitative and qualitative methods simultaneously. According to Sugiyono (2016) mixed methods are methods that combine quantitative and qualitative methods to obtain research data that is more comprehensive, valid, reliable, and objective. The population of this study is unknown therefore the researchers used the Lemeshow formula to determine the sample size. The following is the sample size calculation used in the research using the Lemeshow formula:

$$n = \frac{Za^2 x p x Q}{b^2}$$

Information:

- n = Minimum number of samples required
- Z = Standard value of the distribution according to value=5%=1.96
- P = Prevalence of outcome, because the data is not yet known, 50% is used
- Q = 1-p
- D = The level of accuracy used in this research is 10%

Based on the formula, the calculation of the number of research samples is:

$$n = \frac{1.96^2 x 0.5 x 0.5}{0.1^2}$$

$$n = 96.04$$

From the results of calculations using the Lemeshow formula, the minimum number of samples that must be met is 97 samples. The sampling method in this research used a purposive sampling method. The method chosen is to obtain samples by considering certain criteria set by the researcher. The criteria used to select samples in this research include, the hospitality industry sector in Magelang Regency, which includes hotels, homestays, and Balkondes, serves as the focus of this research. The management of these hospitality businesses is willing to provide the necessary information required by researchers, including data on total assets, leverage, GCG, and financial performance.

The data used in this research are primary and secondary. Primary data through interviews aims to qualitatively analyze data regarding business strategies carried out by the hospitality industry. Meanwhile, secondary data sources come from financial reports recorded by the hospitality industry. To analyze the data, the researchers applied multiple linear regression alongside Moderated Regression Analysis (MRA). Multiple linear regression was used to determine the linear association between the independent variables and the dependent variable. Meanwhile, MRA was employed to explore potential moderating effects by incorporating interaction terms combinations of two or more independent variables into the regression model. This approach allowed the study to evaluate the influence of moderating variables while maintaining the reliability and coherence of the research sample.

4. Results

Table 1 shows the results of the regression analysis on the influence of the DER, Board of Commissioners (*Dewan Komisaris/DK*), Audit Committee (*Komite Audit/KA*), and Institutional Ownership (*Kepemilikan Institusional/KI*) variables on financial performance. The unstandardized coefficient value (B) shows that DER, BOC, and AC each have a positive and significant influence on financial performance, with significance values of 0.001; 0.000; and 0.000, respectively. DER has a coefficient of 5.264, which means that an increase in DER will improve financial performance, while BOC and AC have coefficients of 0.560 and 0.963, respectively. Conversely, IO shows a significant negative influence on financial performance, with a coefficient of -0.417 and a significance value of 0.030. The standardized beta coefficient value shows that the AC variable has the strongest influence in relative terms (0.421), followed by BOC (0.340), DER (0.321), and IO (-0.217).

Table 1. Regression Test

Model	Unstandardized Coefficient		Standardized Coefficients	
	B	Std. Error	Beta	Sig
1(Constant)	0.789	0.193		0.000
DER	5.264	1.494	0.321	0.001
BOC	0.560	0.153	0.340	0.000
AC	0.963	0.225	0.421	0.000
IO	-0.417	0.190	-0.217	0.030

Based on results in Table 1, the regression equation that reflects the variables in this study is:

$$Y = 0.789 + 0.321X_1 + 0.340X_2 + 0.421X_3 - 0.217X_4$$

Description:

Y = Financial Performance

X1 = Leverage

- X2 = Board of Commissioners
- X3 = Audit Committee
- X4 = Institutional Ownership

The results of the t-test reveal that the significance value for the leverage variable is 0.001. Table 2 show the 5% significance threshold (0.001 < 0.05), indicating that the leverage variable has a statistically significant effect. Therefore, the first hypothesis is supported. The results of the t-test show that the significance value for the board of commissioners' variable is 0.000, which is less than the 5% significance level (0.000 < 0.05). This indicates that the board of commissioners exerts a statistically significant influence, thereby confirming the second hypothesis. The t-test results show that the audit committee variable has a significance value of 0.000, which falls below the 5% significance threshold (0.000 < 0.05). This demonstrates that the audit committee has a significant influence on the dependent variable, thus supporting the acceptance of the third hypothesis. The t-test results indicate that the significance value for the institutional ownership variable is 0.030. Since this value is below the 5% significance threshold (0.030 < 0.05), it confirms that institutional ownership has a significant effect, thus supporting the acceptance of the fourth hypothesis.

Table 2. MRA Test

Model	Unstandardized Coefficient		Standardized Coefficients	
	B	Std. Error	Beta	Sig
¹ (Constant)	2.893	0.484		0.000
DER	0.930	2.57	0.055	0.737
BOC	-0.274	0.244	-0.166	0.265
AC	1.092	0.402	0.478	0.008
IO	-1.180	0.334	-0.614	0.001
SIZE	-0.262	0.170	-0.240	0.125
DER*SIZE	-0.203	1.106	-0.082	0.855
BOC *SIZE	0.236	0.092	0.975	0.012
AC *SIZE	-0.287	0.139	-0.918	0.041
IO *SIZE	0.380	0.131	1.248	0.005

Based on the MRA test results Table 2, the regression equation that reflects the variables in this study is:

$$Y = 2.893 + 0.055X1 - 0.166X2 + 0.478X3 - 0.614X4 - 0.240Z - 0.082X1*Z + 0.975X2*Z - 0.918X3*Z + 1.248X4*Z$$

Description:

- Y = Financial Performance
- X1 = Leverage
- X2 = Board of Commissioners
- X3 = Audit Committee
- X4 = Institutional Ownership
- Z = Firm Size

The t-test results reveal that the significance value for the leverage variable is 0.885. Since this value exceeds the 5% significance level (0.885 > 0.05), it suggests that firm size does not moderate the relationship between leverage and financial performance. Therefore, the fifth hypothesis is not supported. The results of the t-test show that the significance value for the board of commissioners' variable is 0.012. As this value is less than the 5% significance level (0.012 < 0.05), it indicates that firm size significantly moderates the relationship between the board of commissioners and financial performance. Therefore, the sixth hypothesis is supported. The t-test results show that the significance value for the audit committee variable is 0.041. Since this value is below the 5% threshold (0.041 < 0.05), it suggests that

firm size moderates the effect of the audit committee on financial performance. Consequently, the sixth hypothesis is accepted. The t-test results indicate that the significance value for the institutional ownership variable is 0.005, which is below the 5% significance level ($0.005 < 0.05$). This finding demonstrates that firm size can moderate the relationship between institutional ownership and the company's financial performance. Therefore, the sixth hypothesis is supported.

Table 3. Regression Determination Coefficient Test

Statistic	Value
R	0.793
R-squared	0.629
Adjusted R Squared	0.616

From the Table 3 it can be seen that the R-square value is 0.629. These results indicate that 62.9% of variations in financial performance can be explained by all independent variables in this study, namely leverage and GCG. While the remaining 37.1% variation in financial performance is explained by other variables outside the research model.

Table 4. MRA Determination Coefficient Test

Statistic	Value
R	0.870
R-squared	0.758
Adjusted R Squared	0.737

Based on the Table 4 the R-square value is 0.758, indicating that 75.8% of the variability in financial performance is accounted for by the independent variables in this study, namely, leverage and GCG with firm size serving as a moderating variable. The remaining 24.2% is attributed to other factors not included in the model. Prior to incorporating the moderating variable, the R-square was 62.9%. Therefore, it can be concluded that the inclusion of firm size as a moderating variable enhances the influence of leverage and GCG on the company's financial performance.

The t-test results reveal several key findings regarding the financial performance of the hospitality industry in Magelang Regency. Leverage significantly influences financial performance ($0.001 < 0.05$), indicating that firms capable of managing their debt efficiently tend to perform better financially. This aligns with the pecking order theory, which suggests that firms relying less on external debt often achieve higher profits. The board of commissioners also shows a significant impact ($0.000 < 0.05$), where a larger board enhances oversight and governance, thus improving performance, in line with agency theory and previous studies. Similarly, the audit committee significantly affects financial performance ($0.000 < 0.05$), as it plays a vital role in reducing stakeholder conflicts through supervision, supporting findings by (Shanti, 2020). Institutional ownership is another influential factor ($0.030 < 0.05$), as it strengthens managerial oversight and minimizes conflicts, thereby improving company outcomes, consistent with agency theory. However, firm size does not moderate the leverage–performance relationship ($0.885 > 0.05$), possibly due to higher debt burdens in larger firms affecting their ability to meet obligations, in accordance with the pecking order theory. Conversely, firm size moderates the impact of the board of commissioners ($0.012 < 0.05$), the audit committee ($0.041 < 0.05$), and institutional ownership ($0.005 < 0.05$) on financial performance. Larger firms, with their broader asset base and wider share distribution, appear to benefit more from effective governance and institutional oversight, ultimately enhancing financial outcomes through reduced agency costs and better asset utilization.

5. Discussion

The findings of this study provide significant insights into the role of leverage and GCG components board of commissioners, audit committee, and institutional ownership on financial performance in the hospitality sector of Magelang Regency, with firm size as a moderating variable. The results reinforce the assumptions of both agency theory and pecking order theory. According to pecking order theory, firms generally prefer internal financing over debt due to lower associated risks, suggesting that low leverage levels may contribute to improved profitability (Ibhagui & Olokoyo, 2018). This theory aligns with the finding that leverage significantly influences financial performance in this context, implying that firms able to manage their debt effectively tend to achieve better financial outcomes. This is in line with the conclusions drawn by Ambarwati et al. (2022), who found leverage to be an important determinant of performance.

The influence of the board of commissioners is also notable. Agency theory posits that effective governance mechanisms help resolve conflicts of interest between management and shareholders. A larger and more independent board can provide stronger oversight, thereby improving managerial accountability and financial outcomes (Jensen & Meckling, 1976; Himawan & Fazriah, 2021). The significant effect observed in this study confirms the role of the board in strengthening governance structures, aligning with research by Widyari et al. (2022), which found similar positive impacts of board oversight on firm performance. Likewise, the audit committee's significant influence on financial performance highlights its role as a core governance mechanism. The audit committee ensures the credibility of financial reporting and strengthens internal controls, which are critical for performance transparency and investor confidence. This is supported by findings from Shanti (2020) and Wulandari and Tan (2023), who emphasize that audit committee effectiveness contributes positively to firm outcomes, particularly when functioning independently and with adequate expertise.

Institutional ownership is another important governance mechanism, as institutional investors often act as external monitors who reduce agency conflicts by supervising managerial behavior. The positive impact found in this study is consistent with Ningsih and Wuryani (2021) and Yusuf et al. (2022), who demonstrated that institutional ownership enhances control and aligns managerial decisions with shareholder interests, thus supporting better financial performance. However, the moderating role of firm size yields more nuanced results. While firm size does not moderate the relationship between leverage and financial performance, it significantly moderates the impact of GCG components board of commissioners, audit committee, and institutional ownership on financial performance. This finding reflects the complexity of larger firms, which may benefit more from structured governance mechanisms due to their scale and resource availability (Prabandari et al., 2023). Larger firms have more extensive operations and, therefore, require stronger governance to mitigate potential inefficiencies and agency issues. This supports the view that firm size amplifies the effectiveness of governance practices in achieving financial goals (Meiyana & Aisyah, 2019).

In contrast, the lack of moderation in the leverage-financial performance relationship suggests that regardless of firm size, debt management remains a consistently critical factor. Larger firms may have more access to capital markets but also face greater financial scrutiny, which can offset any advantages of scale in managing leverage. These findings resonate with studies by Arummingsih (2018) and Antikasari et al. (2020), which showed mixed results in the interplay between leverage, firm size, and financial outcomes. This research contributes to the literature by confirming the critical roles of leverage and corporate governance in enhancing financial performance and highlighting the contextual influence of firm size as a moderator.

6. Conclusion

This study concludes that leverage, the board of commissioners, the audit committee, and institutional ownership significantly influence the financial performance of the hospitality sector in Magelang Regency. Each of these factors plays a distinct role in shaping financial outcomes, aligning with theoretical frameworks such as agency theory and pecking order theory. While leverage directly contributes to performance, governance mechanisms, including the board of commissioners, audit committee, and institutional ownership, are critical in enhancing managerial oversight and accountability, which in turn improve financial results. From a practical standpoint, the findings suggest that hospitality industry stakeholders should emphasize strengthening corporate governance structures and maintain prudent debt management strategies. The evidence that firm size moderates the influence of governance components but not leverage on financial performance implies that larger firms may benefit more from robust governance practices due to their broader scope and complexity. This underscores the importance of tailored governance frameworks for different firm sizes in the hospitality industry.

However, the study is limited by its focus on the hospitality sector within a single region, which may affect the generalizability of the findings to other industries or geographical areas. Additionally, the analysis did not consider non-financial performance metrics, which could provide a more holistic view of organizational effectiveness. For future research, it is recommended to incorporate additional variables such as Corporate Social Responsibility (CSR) and intellectual capital. These factors are believed to play an increasingly important role in influencing company performance, particularly as sustainability and knowledge-based assets gain prominence in strategic decision-making within the service industry.

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Ethical approval was obtained for this study. The manuscript represents original work and has not been previously published, nor is it under consideration by another journal.

Data Disclosure Statement

The data that support the findings of this study are available from the corresponding author upon reasonable request.



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