“Firm value determinants: Reconsidering dividend policy’s moderating role in Indonesia’s top-tier stock index”

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FIRM VALUE DETERMINANTS: RECONSIDERING DIVIDEND POLICY'S MODERATING ROLE IN INDONESIA'S TOP-TIER STOCK INDEX

Abstract

Investors are very interested in companies that have high profits and stable dividend payments. Increasing investment and company profitability increase firm value. This study aims to examine the relationship between liquidity, company size, and earnings quality with firm value and dividend policy as moderators in this relationship. The secondary data used come from the 45 most liquid shares (LQ45) on the Indonesia Stock Exchange and have observations for 10 years from 2014 to 2023. The sample used is 450 data points and is tested using moderated regression analysis. The findings show that earnings quality and liquidity have significant effects on firm value. Conversely, there is no notable effect of firm size on firm value; large assets do not necessarily mean greater firm value if the assets are inefficient. Interactive effect analysis reveals that dividend policy moderates the association between liquidity and firm value, affirming its crucial role in facilitating firm valuation. Also, dividend policy affects the influence of earnings quality on firm value. However, dividend policy does not moderate the relationship between firm size and firm value. Such findings are especially valuable for investors as they indicate that liquid stocks tend to maintain stable dividend payouts, further affirming their value. Moreover, the study suggests that large assets necessarily lead to a greater valuation of a company unless paired with effective management strategies in a volatile business environment.

Keywords dividend policy, liquidity, firm size, earnings quality, firm value

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INTRODUCTION

One of the key achievements of an enterprise is growing the value of the company it owns to date, thereby attracting investors' interest. This means the value of a firm refers to an investor's perception of a company's success and reflects the share price. If a company's values continuously increase, the company could easily face competition. Probably, it means that with the continuously rising firm value, the existence of the company would catch the investors' interest for investment in the top-tier stocks of companies. Investor welfare is an indication that a company can manage resources more effectively and build a good reputation by paying dividends constantly and sustainably (Kashani & Shiri, 2022). Therefore, the dividend function is very important because it can be used to make policies regarding business growth. The dividend policy of any company decides that the earned profits are to be distributed to shareholders in the form of dividends or retained for the shareholders (Abdullah et al., 2023; Seth & Mahenthiran, 2022). A decision to be made between distributing dividends and retaining profits affects the value of a company in the eyes of investors. Distribution of dividends shows the capability of doing good business that will pro-

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duce dividends. A dividend policy is an action that determines the dividend payable on earnings to communicate the profitability, stability, and growth of a company (Momany et al., 2024; Njoku & Lee, 2024). A well-articulated dividend policy would attract investors who focus on regular income and serve as a channel where management can show confidence in the firm's future outlook. On the other hand, the irregularity of a badly communicated dividend policy would most probably raise questions over the value of a company perceived by an investor. While high performance would attract investors to invest in companies to get an idea of the value of the firm.

1. LITERATURE REVIEW

Liquidity describes the ability of an organization to meet its maturing short-term obligations from its existing or current assets. It depicts good management of current assets through efficient handling of the firm's short-term liabilities (Almakura et al., 2024; Liu & Suzuki, 2024). High liquidity depicts a situation of financial stability and efficiency in operation; these factors could give investors confidence in the firm and therefore affect the value of the firm positively. It is based on empirical evidence that highly liquid firms, on the one hand, are associated with high market valuation. This, in turn, can increase the price of the firm shares and hence the value. Consequently, from the above discussion, the signaling theory asserts that investors need the availability of liquidity measures for decision-making on firm value since good liquidity proposes positive signals to shareholders concerning the stability and reliability of the firm. Besides, high liquidity levels imply more transparency with low information asymmetry between shareholders and executives. This means shareholders are more capable of judging the liquidity position of a corporation and, thus, make more informed decisions about their investments. The general outcome, therefore, thanks to the alignment of interests of shareholders and executives, will reduce agency costs and increase value-added. It is not only very important for companies to improve liquidity performance, but also to obtain a strong signal of financial stability that attracts investor interest and thereby increases firm value. The relationship has been further explained under the agency theory. Agency theory indicates a conflict of interest between the principal and agent, who are usually the shareholders and company executives. They may prefer personal goals at the expense of the financial health of a company, hence bringing inefficiency in the management of such assets. Results from some of the previous studies, as given by Cahyani et al (2023), record increased firm value with an increased liquidity level. Wirama et al. (2024) proved the positive impact of liquidity on firm value, and it has been proven that this is happening in Indonesian firms. The conflict may be reduced if the liquidity level is high since there will be adequate current assets to meet short-term obligations, and hence the probability of financial distress will be minimized.

Company size is measured by the size of assets and sales. The larger the company, the more stable the condition, which reflects high firm value (Cahyani et al., 2023; Radja et al., 2020; Hashmi et al., 2020). Hence, in this case, firm value can be measured by the firm size and associated with the signaling theory for making investment decisions. Certain studies by Ardelia et al. (2024) and Dang et al. (2019) derived the conclusion that firm value is related to company size. Large-scale business indicators, such as total equity, sales revenue, and assets, attract investors. Investors are, therefore, more likely to invest in bigger companies that usually operate in more stable business environments under varying economic conditions (Daromes et al., 2022). Again, the issue is well explained by the agency theory. Large firms possess large size and resource characteristics; it can, therefore, be argued that such firms could establish governance arrangements that minimize this interesting conflict between the two groups. The reduction in agency costs means an improvement in governance because managers then act to promote the interests of shareholders via enhanced firm value (Nguyen et al., 2020). The findings by Cahyani et al. (2023) verify this view that the size or value of firms have a positive and significant effect.

Earnings quality depicts the reliability and accuracy of the reported earnings, reflecting an entity's true financial performance. High-quality earnings are transparent and reliable information provided

to investors, enhancing investors' confidence and, in turn, the value of a firm (Vintilă, 2024). The profit reports exhibit high qualities as they facilitate users' decisions and explain stock prices. It follows that a firm's value appreciates with an increase in the share price, which is taken as an indicator of firm value. As the theory of signaling maintains, high earnings quality sends positive signals to shareholders, reflecting the good financial health and stability of a company. The relation between earnings quality and the value of a firm may be asymmetrically informed. Asymmetric information exists under conditions when the parties do not have an equal level of information. In most cases, it exists between the company's executives and shareholders. Good earnings reports will mitigate the asymmetric information problem where business owners are provided with appropriate and transparent financial information (Darminto et al., 2024; Li et al., 2023). Optimal investment decisions are realized when owners have reliable information since there is limited uncertainty and risks of adverse selection. Agency theory further supports this relationship. It resolves a conflict of interest for principals and agents represented through shareholders and company executives. High-quality earnings reports help align their interest, reducing information asymmetry and ensuring transparency. This kind of transparency reduces agency costs since these shareholders can then monitor and better evaluate executive performance. Improved quality of earnings encourages investor confidence and directs management activities to be in line with shareholders' interests in increasing the firm's value. This has been observed by Duarte et al. (2024) and Intara et al. (2024). The support for such studies, as follows, gives the positive effect of earnings quality on firm value (Khan & Shoaib, 2024; Fassas et al., 2023). Thus, high earnings quality is very crucial for a firm to signal financial health and information asymmetry low enough to invite investor interest in enhancing firm value.

Large firms with more resources and market presence offer stability and attract investors, adding to firm value. High-quality earnings also signify reliable and accurate financial reporting and attract investors because they reflect transparency and good health in terms of finances. Besides, the dividend policy is a moderator in these relationships and further influences firm value through the distribution of part of the earnings to shareholders, hence boosting investor confidence (Abdullah et al., 2023). From this point of view, Bahraini et al. (2021) confirm the said relations and pinpoint that dividend policy, together with liquidity, firm size, and earnings quality, considerably affect the value of firms. Besides, a so-called agency theory can explain how the above-mentioned variables might mitigate contradictions of interests among shareholders and top managers. Liquidity sufficiency to meet all obligations, already established governance structures of large firms, and high quality of earnings reduce asymmetry in information, combining the alignment of interest and promotion of firm value (Brigham & Houston, 2015). Shortly, high liquidity, large enterprise size, good quality of earnings, and effective dividend policy are the guarantees of signals of financial stability that draw the attention of investors to create value. Another role that dividend policy plays in the nexus of liquidity-firm size-earnings quality-firm value is a moderating one, given that it has major implications for investor perceptions about a firm's current financial health and its prospects.

High liquidity would hint at good health and thus perhaps become a factor attractive to investors, increasing firm value. The above, put together with one continued policy of dividend payment, will show there is adequate liquidity for the needs of the firm's growth in operation to satisfy increased operational activities as well as investor returns and growth, thereby increasing the confidence of investors (Lin & Lee, 2021; Widyakto et al., 2024). Larger firms possess all the resources and market standing, and hence would be more attractive to investors who seek stability. These same companies would then make a firm's value increase because a stable dividend policy gives investors some confidence in regular income and commitment to shareholder returns (Booth & Zhou, 2017; Chen et al., 2022). High-quality earnings send out signals of transparency and reliability in financial reporting; this attracts investors because it reflects strong financial health. The commitment is towards the return of profit and hence would increase firm value if such a dividend policy is established where some portion of high-quality earnings goes to the shareholder (Dixit et al., 2020; Wirama et al., 2024). Evidence of such associations is supported

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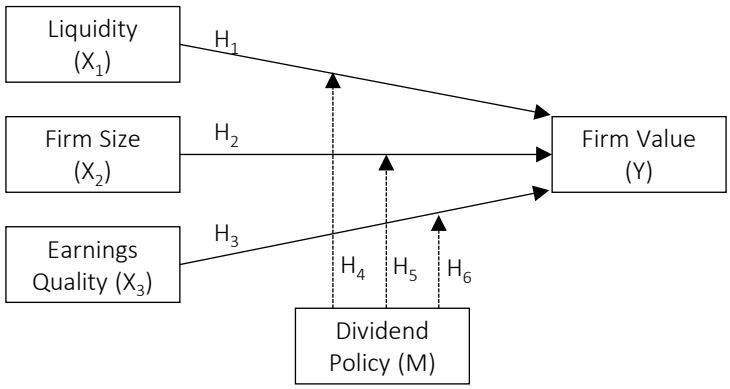

Figure 1. Research framework

by studies indicating that, besides liquidity, firm size, and quality of earnings, dividend policy is a significant factor influencing the value of a firm by aligning the interests of shareholders and executives, reducing conflicts of interest, and securing financial transparency and stability that raise investor confidence in the value of the firm.

Dividend policy has been among the value determinants of a firm for many years. Dividend policy is also found to be related to firm value positively, especially in emerging nations; it can serve the function of financial signaling in augmenting the link between earnings quality and firm value (Prasojoharto et al., 2024; Bakri, 2021). In addition, dividend policy is also an intervening variable to bolster the relationship between the mechanism of earnings quality and firm value. According to a study by Said (2024), high earnings quality is a good signal to investors, therefore increasing the value of the company. In addition, a study by Chakkravarthy et al. (2023) suggests that dividend policy can moderate the relationship between earnings quality and firm value, especially for firms with complex ownership. Thus, dividend policy as a moderating variable plays a role in analyzing the effect of earnings quality on firm value and exploring the relationship.

The literature has described liquidity, firm size, and quality of earnings as fundamental determinants of firm value, and dividend policy as a fundamental moderating variable. Empirical research consistently reveals that financially more liquid firms are considered financially stable and best positioned to fulfill their debt obligations, thus attracting investors and increasing firm value. Similarly, larger firms with greater resources and market influence provide stability and are therefore appealing to investors who desire long-term security. Earnings quality also further induces investor confidence by referring to clean financial reporting and efficient operations, supporting firm value.

Dividend policy plays a dual role in this dynamic, both as an additive that positively contributes to firm value on its own and as a moderator that increases the impact of liquidity and earnings quality on firm valuation. A healthy and stable dividend policy sends a signal of health, reducing information asymmetry and aligning the interests of shareholders and executives. Past studies reveal that dividend policy not only has direct effects on firm value but also serves as a tool for improving investors' perception of a firm's financial health and future, particularly in emerging markets. Financial transparency, good governance, and stable dividend payments are recognized throughout the literature as the key features for sustaining investor confidence and firm valuation.

As such, this study has sought to empirically examine the direct effects of liquidity, firm size, and earnings quality on firm value and assess the moderating role of dividend policy in this context. The research hypotheses are:

H_1: *Liquidity has a positive effect on firm value.*

H_2: *Firm size has a positive effect on firm value.*

H_3: *Earnings quality has a positive influence on firm value.*

H_4: *Dividend policy moderates the relationship between liquidity and firm value.*

H_5: *Dividend policy moderates the relationship between firm size and firm value.*

H_6: *Dividend policy moderates the relationship between earnings quality and firm value.*

2. METHODS

Companies listed in the LQ-45 index on the Indonesia Stock Exchange (BEI) from 2014 to 2023 have provided official information via the Indonesia Stock Exchange website (Luthfia et al., 2024). Secondary data used in this research are company financial reports. The population and sample are derived through a purposive sampling method. The research sampled the population using the data of companies listed in the LQ-45 index on the Indonesia Stock Exchange BEI 2014-2023, while in the found, during the 45 samples of this period, there exist 10 consecutive years ranging from 2014 to 2023, totaling 450 statements (https://www.idx.co.id/en/listed-companies/financial-statements-and-annual-report). Purposive sampling techniques shall be performed within this study. The following are some of the sample selection criteria used in this study: 1) The company is listed in the Indonesia Stock Exchange LQ-45 Index https://www.idx.co.id/id/data-pasar/data-saham/indeks-saham/ 2) The currency of the financial statement is in rupiah; 3) During the research period, the company did not experience losses; 4) The company has audited annual financial report data; and 5) During the research period, the company did not get delisted from the Indonesian Stock Exchange. This study uses secondary data sources. A secondary source of material used within a research setting would include annual financial reports listed on the Indonesia Stock Exchange from 2014 to 2023. The normality test and dependent variable being analyzed in a regression equation model follow a normal distribution or otherwise is presented, based on Pituch and Stevens (2015) a probability value above the 5% significance level is normal, and below 5% is abnormal. A multicollinearity test was necessary to define whether independent variables were related among themselves or to dependent variables. If there is no correlation between the independent variables, the research variable is considered good. If the tolerability value is > 0.1 or equal to VIF < 10, the regression model is considered free of multicollinearity. The heteroscedasticity test is an assumption test intended to determine whether there is a difference in variance between the residuals from one observation to another. There is no heteroscedasticity in cases where the variable significance probability value is greater than 5%. Vice versa. This study uses multiple regression equations to analyze the influence of liquidity, company size, earnings quality, and dividend policy on firm value. Moderating regression analysis was used to determine the moderating role of dividend policy. The multiple regression equation model 1 and the moderating regression analysis model 2 are described in formula form as follows:

Model 1: The multiple regression analysis:

$$Y = a + b_1X_1 + b_2X_2 + b_3X_3 + e, \quad (1)$$

Model 2: The moderating regression analysis

$$Y = a + b_1X_1 \cdot M + b_2X_2 \cdot M + b_3X_3 \cdot M + e, \quad (2)$$

Y – Firm value, a – Constant value (price of Y when X=0), $b_{1,2,3}$ – Regression coefficient values, X_1 – Liquidity variable, X_2 – Company size variable, X_3 – Earnings quality variable, M – Dividend policy variable, e – Standard error.

Table 1. Variable proxy and measurement

Variable	Proxy	Formula
Liquidity (X_1)	Current ratio (CR)	$\frac{\text{Current assets}}{\text{Current liabilities}}$ x 100%
Firm size (X_2)	Natural Logarithm of Total Assets	Ln Total asset
Earnings quality (X_3)	Quality of earnings ratio (QoE)	$\frac{\text{Cash from operation activity}}{\text{Net income}}$
Dividend policy (M)	Dividend payout ratio (DPR)	$\frac{\text{Total dividend paid}}{\text{Net income}}$
Firm value (Y)	Price earnings ratio (PER)	$\frac{\text{Market price per share}}{\text{Earnings per share}}$

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3. RESULTS AND DISCUSSION

The normality tests in Table 2, autocorrelation tests, multicollinearity tests, and heteroscedasticity tests are classical assumption tests conducted to make sure that a good regression model is formed. From the normality test results using the One-Sample Kolmogorov-Smirnov test, the Asymp. Sig. value in model 1 was 0.91, and in model 2 it was 0.65. This value was >0.05, and it can be concluded that the data are normally distributed (Pituch & Stevens, 2015).

Table 2. Normality test

Model	N	Asymp.Sig	Conclusion
1	450	0.91	Normal Distributed
2	450	0.65	Normal Distributed

From Model 1, it is observed that VIF for all variables, such as Liquidity, Firm Size, and Earnings Quality, is less than 10, and tolerance is more than 0.1. Hence, there is no multicollinearity, which implies that all these variables are not highly interrelated, and the regression model is stable.

Model 2 includes interaction terms: Liquidity*Dividend Policy, Firm Size*Dividend Policy, and Earnings Quality*Dividend Policy. The VIF increased for some variables, for instance, liquidity and earnings quality, as well as for interaction with the Dividend Policy. Nevertheless, all the variables still indicate no multicollinearity. The magnitude of VIF stands below the critical level of 10; thus, it is still reliable that the regression model has no severe multicollinearity problems (Table 3).

All the variables' significance values (Sig.) are above the general threshold value of 0.05, reflecting no evidence of heteroscedasticity (Table 4). That is, the residuals of this regression model are homoscedastic; this means that the variance is constant, which is desirable to achieve for model stability and reliability.

Table 5. Autocorrelation test

Model	Durbin-Watson	Conclusion
Model 1	1.471	Free autocorrelation
Model 2	2.073	Free autocorrelation

In the first and second models (Table 5), Durbin-Watson statistics fall within ranges generally acceptable. This is typically between 1.5 and 2.5, meaning that these residuals do not have an issue of substantial autocorrelation. Otherwise put, these are independent errors of regression; thus, these do not correlate with one another through time. From Tables 3 and 4, the regression models

Table 3. Multicollinearity test

Model	Variable	Tolerance	VIF	Conclusion
Model 1	Liquidity	0.724	1.316	No multicollinearity
	Firm Size	0.780	1.301	No multicollinearity
	Earnings Quality	0.814	1.211	No multicollinearity
Model 2	Liquidity	0.229	4.217	No multicollinearity
	Firm Size	0.783	1.296	No multicollinearity
	Earnings Quality	0.241	4.194	No multicollinearity
	Liquidity*Dividend Policy	0.275	3.699	No multicollinearity
	Firm Size*Dividend Policy	0.174	5.689	No multicollinearity
	Earnings Quality*Dividend Policy	0.283	4.207	No multicollinearity

Table 4. Heteroscedasticity test

Model	Variable	Sig	Conclusion
Model 1	Liquidity	0.717	No heteroscedasticity
	Firm Size	0.725	No heteroscedasticity
	Earnings Quality	0.790	No heteroscedasticity
Model 2	Liquidity	0.237	No heteroscedasticity
	Firm Size	0.771	No heteroscedasticity
	Earnings Quality	0.237	No heteroscedasticity
	Liquidity*Dividend Policy	0.293	No heteroscedasticity
	Firm Size*Dividend Policy	0.279	No heteroscedasticity
	Earnings Quality*Dividend Policy	0.307	No heteroscedasticity

have passed tests for heteroscedasticity and autocorrelation, going ahead to ensure the stability and reliability of the models.

Table 6. Coefficient of determination

Model	Adjusted R-Squared
Model 1	0.419
Model 2	0.389

Table 6 illustrates that Model 1 – The Adjusted R-Square = 0.419, roughly 41.9% variation of the dependent variable would be accounted for by the independent variables with Model 1. Model 2 – The Adjusted R-Squared = 0.389, roughly 38.9% variation of the dependent variable would be accounted for by the independent variables under Model 2.

Table 7. F-statistical test

Model	F-Count	Significant Value
Model 1	32.472	0.000
Model 2	21.822	0.000

Model 1 in Table 7, the F-Count comes out to be 32.472 with a Significant Value of 0.000. This shows that the overall regression model is statistically significant, which means it makes a claim that the independent variables taken as a whole considerably affect the dependent variable. F-Count in model 2 amounts to 21.822 with a Significant Value of 0.000. This also supports the fact that the overall regression model is statistically significant, meaning that taken as a whole, the independent variables have a significant effect on the dependent variable.

Model 1 in Table 8 presents the output of the multiple regression analysis test. The constant has a positive coefficient value of 2.947 and is statistically significant, with Sig = 0.004. This indicates that there is sufficient evidence to prove the effect of the constant on firm value within the model. The coefficient of liquidity is 0.452 and statistically significant at Sig = 0.000. This implies that liquidity significantly and positively influences firm value. The coefficient for firm size is 0.139 but insignificant at Sig = 0.629. Thus, firm size is not a significant determinant of the firm value variable. The coefficient for earnings quality is 0.178 and statistically significant at Sig = 0.010. That means, the better the earnings quality, the higher the increase in firm value by 0.178 units. Earnings quality positively affects the firm value. Model 2 presents the result of a moderating regression analysis.

The constant coefficient is 2.537. Its Sig. = 0.002, which means statistically significant. Thus, the constant is a significant determining factor in this model. The interaction term is with a positive coefficient of 2.844 and statistically significant since Sig = 0.000, which indicates that the effect of liquidity on the dependent variable is moderated by dividend policy in an enhancing way. The coefficient for this interaction term is 0.009; however, it is insignificant since the significance level is 0.179. The dividend policy has an insignificant moderating effect on the relationship between firm size and the dependent variable. The interaction term's coefficient is 0.038, and it is statistically significant with Sig=0.037. This, therefore, means that dividend policy is the moderating variable of the quality of earnings to the dependent variable, but it has relatively insignificant effects. Therefore, from Model 1, liquidity, earnings quality, and dividend policy were the significant predictors of the dependent variable. In Model 2, the interaction of dividend policy with liquidity and with earnings quality in influencing the dependent variable is highly significant, though the former is stronger than the latter.

Table 8. T-statistical test

Model	Hypothesis	Variable	Unstandardized Coef. Beta	T Statistic	Sig	Conclusion
Constant			2.947	2.827	0.004	
Model 1	H_1	Liquidity	0.452	5.193	0.000	Accepted
	H_2	Firm Size	0.139	0.160	0.629	Rejected
	H_3	Earnings Quality	0.178	2.517	0.010	Accepted
Constant			2.537	2.586	0.002	
Model 2	H_4	Liquidity* Dividend Policy	2.844	3.746	0.000	Accepted
	H_5	Firm Size* Dividend Policy	0.009	1.351	0.179	Rejected
	H_6	Earnings Quality* Dividend Policy	0.038	0.583	0.037	Accepted

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4. DISCUSSION

The outcome of the analysis reveals that liquidity is very critical and greatly beneficial. This result has demonstrated the role of liquidity within the model and, thus, highlights that such firms, which have a greater level of liquidity, can meet the needs of their short-term needs as well as obtain better opportunities. Higher liquidity would mean that a firm can maintain enough liquid resources to settle its current liabilities, enhancing financial solidity and buffer capacity in business activities. Liquid companies can sustain business activities during economic recessions and are able to carry out business activities even during a recession. This finding is also in concurrence with Bidaya et al. (2023), who assert that more liquid companies are better off in terms of financial performance and vulnerability to financial distress. However, while earlier research mostly emphasizes the role of liquidity in financial stability, this study continues to show its role in firm valuation, and it suggests that liquidity is not only a guarantee against financial distress but also a fundamental driver of firm value.

According to MPT, liquidity is among the main components of a portfolio because it allows underlying assets to be sold at very short notice and at negligible value decay so that businesses can effectively exploit market volatility. The implicit agenda of the MPT assumes that diversified portfolios will hold highly liquid assets to reduce risk as well as optimize returns (Trisnawati et al., 2024). This study validates the relevance of MPT in corporate finance as it empirically establishes that highly liquid companies grow increasingly attractive because they are able to adjust financial policies quickly based on the market conditions. Previous research, such as Cahyani et al. (2023), emphasizes liquidity management as a finance policy, but the current study extends that by emphasizing liquidity as a factor in determining firm valuation, particularly in firms with fixed dividend policies.

The findings ultimately validate previous research conducted on the role and significance of liquidity in corporate finance. Bidaya et al. (2023) find that more liquid firms achieve better financial performance and less financial distress risk, whereas Cahyani et al. (2023) further emphasize the importance of managing liquidity in maintaining firm value. However, the results of this study highlight that liquidity, beyond being a determinant of financial stability, has a direct impact on influencing investor confidence and valuation, which has been less studied in previous work. The model would therefore suggest, with regard to liquidity, that managers and investors should prioritize having sufficient liquid funds in a position to invest in strategic initiatives and short-term obligations. This also means that firms that have sufficient liquidity are able to effectively seize new opportunities, negotiate good credit terms, and hedge against risk in periods of economic turmoil. While earlier research emphasizes liquidity as a risk management tool, our study upholds its intense role to increase firm value in support of the underlying assumption of the Modern Portfolio Theory that liquidity is an important variable influencing financial stability, firm value, and investors' confidence.

Firm size, while significant elsewhere, plays no significant role here. This can be taken to imply that, except for firm size, other variables play a greater role in the determination of firm value. Although firm size is generally associated with a variety of advantages, e.g., economies of scale, better access to capital, and increased market power, none are especially strong enough to exert an effective impact on the explanatory power of the model in this sense. This fits with the Agency Theory, which supposes that managerial inefficiencies and conflicts of agency can prevent a firm from being able to delineate the performance or value of the firm. Unlike Ardelia et al. (2024) and Dang et al. (2019), who emphasized the resource advantage of bigger companies, this paper also presents additional evidence that inefficiencies and governance factors may offset benefits from firm size. Therefore, rather than focusing on growth alone, companies may emphasize maximizing internal processes so as to create maximum efficiency for managerial roles, thereby minimizing agency conflict and improving performance (Daromes et al., 2022; Radja et al., 2020). An emphasis on good corporate governance practices, a culture of accountability, and aligning managerial interests with shareholder objectives can minimize such inefficiencies and maximize firm value.

Earnings quality positively affects its presence in the model. Firms with good earnings quality provide more reliable financial information that improves the explanatory power of firm value models. Good earnings display truthful financial reporting without distortion or manipulation, thereby improving investor trust and enabling informed decisions. The Efficient Market Hypothesis argues that highly well-informed markets embed earnings quality within security prices, supporting financial openness, enhancing investor trust. Unlike Khan and Shoaib (2024) and Fassas et al. (2023), who primarily emphasize earnings quality as a stock performance determinant, this study also emphasizes its explicit contribution to the valuation of companies through improving financial credibility and investor confidence. The preservation of high-quality earnings through rigorous internal controls, stringent accounting standards, and transparency culture is essential in the sustenance of bolstered financial reports and a positive image in the market. Companies have to continuously enhance their financial reporting frameworks to remain transparent, thus creating an investment-conducive environment and raising their long-term valuation.

The interaction between dividend policy and liquidity is very positive and highly influential, showing the collective impact of these two in making a firm more attractive (Azmi & Bertuah, 2020; Bhattacharya et al., 2020). The findings indicate that firms with sound liquidity management and consistent dividend policies are considered to be more financially strong and therefore more appealing to investors (Li et al., 2023). In contrast to the current literature, which mainly examines liquidity and dividend policy separately, this study contributes to the literature by demonstrating the powerful joint influence of both on firm valuation. The connection between firm size and dividend policy is not significant, i.e., investors do not prioritize firm size when making decisions concerning dividend policies (El-Deeb & Allam, 2024). This aligns with the assumption of Behavioral Finance Theory that investors are more concerned with dividend stability than with firm size, which supports the argument that investor sentiment has a greater impact on firm valuation than organizational size. Earnings quality and dividend policy interaction terms provide further evidence that high-quality financial reporting and consistent dividend payments have positive and significant effects on firm value (Fitri et al., 2024; Shubita et al., 2024). While previous research primarily accounts for the individual effects of earnings quality and dividend policy, the present study highlights their complementary role in shaping investor opinions and firm valuation overall (Mutmainah & Akhmadi, 2024). Companies that are open and committed to consistent dividends will be perceived as stronger and more credible, adhering to Value Investing principles that emphasize the quality earnings and consistent dividend payments as major determinants of stock value.

CONCLUSION

This study investigates the determinants of firm value and the role of dividend policy in the LQ 45 index in Indonesia. The analysis indicates that liquidity is highly positively significant in the model. This points to the reality that the maintenance of adequate liquidity is highly important for companies because this bolsters the ability of such entities to meet their short-term obligations and window opportunities. While firm size may be relevant in other contexts, it is not in this model. The fact that the influence of quality earnings significantly shows its importance in this model. High-quality earnings provide better information for making rational decisions and attracting investors' confidence. The dividend policy also contributes very positively to this model. Companies with stable dividend policies are considered more stable and, therefore, more appealing to investors. These results point to the fact that a reliable dividend policy is of prime importance and acts as the highest means to the improvement of investor confidence and firm valuation. The interaction effects of liquidity and dividend policy and those of earnings quality and dividend policy are highly significant. It reflects that the combined effect of variables exerts more influence than the contribution of individual ones. Moreover, the large interaction effects observed provide new insights into their combined effect and point to significant added value by considering multiple factors in financial models. Besides, the period analyzed might have undergone

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peculiar market conditions that would consequently give out biased results, while different economic environments may show different results. Future research in this direction can go a step further in exploiting other variables and their interactions to have a wider understanding of the factors affecting firm performance. Cross-country analysis would thus compare the results against different countries and economic environments, bringing out both universal and context-specific factors that impact financial performance.

AUTHOR CONTRIBUTIONS

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