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Corporate Governance and Profitability: The Role of Cost of Capital as Mediation

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Abstract
This study aims to analyze the effect of internal corporate governance mechanisms with the cost of capital as mediating variable and profitability as a dependent variable in companies listed on the Indonesia Stock Exchange during period 2015 to 2020. This study uses secondary data collected from Bloomberg's financial data and the company's annual report. A total of 807 companies as a population by sampling with purposive sampling method in order to obtain 300 companies from various sectors. The analysis method employs a structural equation model Structural Equation Modeling (SEM) based on the Partial Least Square (PLS). Based on hypothesis testing through the t-statistical test with a bootstrapping method, the results show that corporate governance has a positive relationship with profitability, and the cost of capital has a fully mediating role in the relationship between corporate governance and profitability.

Keywords: Corporate governance, profitability, cost of capital, growth
JEL Classification: G3, G21

1. INTRODUCTION

The era of Globalization affects various structures of life, including the business world. Progress in the business world, one of which is characterized by the high influence of globalization, companies are required to be able to compete competitively with other companies where they must adjust to the circumstances that are happening and be able to manage the important functions of the company. Several strategies are carried out by companies to show their extension in the world of the industry being run, because each company expects its company to run well financially and non-financially. An important end goal for the company is to obtain the maximum profit or profit as targeted. In a management company, it is required to be able to meet the targets that have been set (Kasmir, 2019).

Maintaining the company's survival, one of them is by increasing profitability. With profitability, the welfare of the company can be achieved because it is used to measure performance in a company (Narwal & Pathneja, 2016). Return On Asset (ROA), Return On Equity (ROE), and Return On Investment (ROI) are financial ratios used to measure a company's profitability. The measurement results of this ratio can be used as a tool for evaluating the performance of management has worked effectively or not (Kasmir, 2019). One of the goals of an enterprise is to achieve maximum profitability. With a high return, it will support investors to invest in the company, so good corporate governance is needed to fulfill all rights for all stakeholders and avoid agency conflicts. In addition, good corporate governance can minimize risks in the company (Ofoeda, 2017). Therefore, corporate governance is one of the factors that affect profitability.

The implementation of good corporate governance, it will improve the company's performance because the decisdecision-makingess is carried out properly by synergizing with each other between stakeholders in accordance with the applicable provisions of the company. This shows the relationship between corporate governance and profitability. According to Sheikh & Wang, (2012) corporate governance explains the relationship between various forms of participants in the company whose purpose is to determine the direction of company performance. The need for good corporate governance arises in relation to principal-agency theory, namely to avoid conflicts between principals and agents. The conflict arises because of differences in interests that must be managed so as not to cause harm to the parties concerned. To create good corporate governance, mechanisms are used in its application consisting of internal mechanisms and external mechanisms. The size of the board of directors, board of commissioners, and independent commissionersiss a component of the internal mechanism of managing the company.

The Board of Commissionersiss an internal control mechanism that is responsible for supervising and providing solutions to the board of directors (Melanthon, 2017). The Board of Commissioners is a corporate organ that has an important role in the implementation of corporate governance,and holds the task of ensuring the implementation of activities, supervising operational management, and ensuring accountability. This shows that the board of commissioners is at the core of the implementation of corporate governance. Independent commissioners are tasked with ensuring that supervisory activities by the board of commissioners run effectively and in accordance with applicable regulations. So that in the existence of an independent commissio, it can minimize supervisory errors from commissioners related to company activities which will later affect the company's performance. The board of directors is the total number of directors in one board of the company as the executor of the operation and management of the company. The board of directors becomes an important part of governance because they control the company's operations and strategic decisions (W. Sheikh & Alom, 2021).

In a study, a positive relationship was found between corporate governance, namely the size of the board of directo,rs with ROA and ROE (bank performance). When there is a change in uniin, the size of the board of directors can increase by 2 to 8 percent return on assets and return on equity (Emmanuel & Riman, 2012). On the other hand, there is a finding that the size of the board in the company contributes negatively to the company's performance. The larger the size of the board, the performance of the company will decre,asehat it should not be in the company of too many bboards(Amran, 2011; Habib, 2016).

Company managers are the parties who play the most role in determining the company's funding alternatives. The selection of alternative sources of funds in the trade-off theory is based on consideration of costs and benefits arising from the use of debt, so the management must make the right decisions in the selection of capital structures. It says the capital structure is optimal when it can minimize the overall cost of using capital or the weighted average cost of capital the company's low capital costs will increase the company's profit,s and vice ver. Ifif the cost of capital is greater, it will reduce the company's profits because the company's profits are affected by the costs incurred by the company. The cost of capital refers to the financial costs borne by the company and the minimum amount of expected return that the investment project must obtain in order to increase the value of the enterprise. Cormier et al., (2010) examined the role of corporate governance in reducing information asymmetry resulting in that voluntary corporate disclosure would reduce information asymmetry between managers and investors. Broader disclosure will increase stock market liquidity, thereby lowering the cost of capital either lowering transaction costs or increasing demand for corporate securities (Lahaya, 2017).

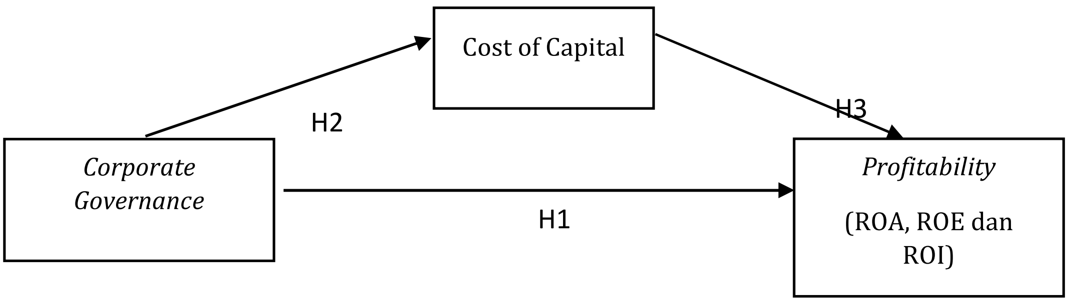
Based on previous theories and studies, researchers found an indirect relationship between corporate governance and profitability. There are concretely invisible intermediaries that can affect corporate governance relations to the company's profitability. Mediation variables are used to explain the indirect relationship between independent variables, namely the board of directors, the board of commissioners, and independent commissioners as part of corporate governance, and the dependent variables, namely return on assets, return on equity and return on investment in measuring the company's profitability. Theoretically, the application of good corporate governance lowers the cost of corporate capital where transparency and disclosure will reduce transaction costs because stock market liquidity increases (Diamond & Verrecchia, 1991).). Such low capital costs will increase the company's profits because management establishes an optimal capital structure. Implicitly, the cost of capital affects corporate governance on the company's profitability indirectly. Therefore researchers use the variable cost of capital as a mediator in the study.

Some literature proves how a company's profitability is affected by good corporate governance practices and the cost of capital associated with its funding decisions. But there are still few researchers who test the role of the cost of capital itself in relation to corporate governance and profitability. This research is an effort to investigate the impact of corporate governance in generating profits for companies by examining the role of capital cost mediation in the relationship between corporate governance and profitability in companies listed on the Indonesia Stock Exchange from 2015 to 2020.

2. HYPOTHESIS DEVELOPMENT

The practice of corporate governance cannot be separated from agency theory and stewardship theory. Agency theory looks at conflicts of interest arising from possible differences between principals (shareholders) and agents (managers) of the company. Such agency matters give rise to agency costs relating to monitoring costs and other costs by agents to reassure shareholders that it will not harm their interests. Self-serving managerial behaviors such as negligence, consumption of additional income, increasing compensation, and reducing the risk of work resulting in losses to shareholders (Jensen & Meckling, 1976). According to stewardship theory, the behavior of the stewardship is collective, since the steward is trying to achieve the goals of the organization (for example, sales growth or profitability). This behavior will in turn benefit principals such as outside owners (through the positive effect of profits on dividends and stock prices) and also principals who are managerial superiors, since their goals are followed up by servants.

Stewardship theory assumes managers will behave in the interests of the company. When the interests of the steward and the owner are not the same, the steward will try to cooperate rather than oppose it, because the steward feels that the common interest and behaving in accordance with the behavior of the owner is a rational consideration to achieve the goals of the company so as to improve the welfare of the principal and other stakeholders. In this theory, the application of good corporate governance will affect the company's profitability. When the corporate governance system is weak, inadequate monitoring and control, information asymmetry, and agency conflicts give rise to self-serving internal management activities, such as excessive borrowing and expansion of compensation benefits and benefits. If management does not choose a strategy of maximizing value, the exposure of market risks for the company increases, which poses systematic risks and ultimately increases the cost of capital (Kien et al., 2004). High cost of capital will reduce profitability where transaction costs increase as stock market liquidity decreases.



Source: Hayes, (2018)

Figure 1. Research Framework of Thought

The Effect of Corporate Governance on Profitability

The basis of corporate governance is to promote transparency, fairness, accountability and direct company management to act in accordance with the provisions. Emmanuel & Riman, (2012) conducted a study on the effect of corporate governance on profitability in banking sector companies in Nigeria. The research resulted in a fairly good relationship between corporate governance and bank performance because changes in units in the size of the board of directors and the size of shareholders can increase return on assets (ROA) and return on equity (ROE). It is not the total amount of assets or equity that determines the performance of the bank but rather the quality of the assets, equity providers and the management of corporate governance that affects the performance of the bank. Corporate governance mechanisms proxied by the size of the board of commissioners are able to encourage managers to increase company profits (Mai, 2015). The study is in line with Danoshana & Ravivathani, (2013); Iqbal & Kakakhel, (2016). The researcher Ademola et al., (2016); Frumentius & Christiawan, (2020); Hardiyawan et al., (2015); Pasaribu & Simatupang, (2019); dan W. Sheikh & Alom, (2021)also found that corporate governance has a positive effect on financial performance.

Profitability is the financial result of a company that can be measured through revenues and costs (Frumentius & Christiawan, 2020). On the other hand, research conducted by Zabri et al., (2016)showed a significant negative relationship with financial performance as measured by Return On Asset. The study was conducted on public companies in Bursa Malaysia using corporate governance indicators of board independence board size. These results are consistent with studies on corporate governance in China Peng et al., (2021)and supported by research by Arora & Sharma, (2016);

Frumentius & Christiawan, (2020); dan Habib, (2016) therefore, on the basis of the literature proposed hypothesis:

H_1: Corporate governance has a positive effect on the profitability of the company.

The Effect of Corporate Governance on Costs of Capital

Bad corporate governance mechanisms can lead to deficiencies in the company's transparency and disclosure practices, leading to an increase in issuance costs and other transaction costs. This will increase the company's capital costs further. Many studies, including Botosan, (1997); Botosan & Plumlee, (2002) have investigated the dimensions of governance disclosure and their impact on the cost of debt financing as well as the cost of equity financing. The researcher concluded that by reducing the level of information asymmetry between investors and managers, then the cost of capital will decrease. Other researchers such as Ashbaugh et al., (2004); and Chen et al., (2003) examined the effect of other governance mechanisms on the cost of equity capital. Companies can influence the level of equity capital costs by minimizing the level of information asymmetry through the expansion of voluntary disclosures, the low asymmetry of information increases investors' sense of security and confidence in the company in its investments (Lahaya, 2017). Chen et al., (2003) concluded that the impact of corporate governance mechanisms on the cost of equality is more noticeable in regimes with inadequate legal protections and weak regulatory frameworks. Contrary to this, Zhu, (2012) presents evidence of the strong impact of corporate governance mechanisms on the cost of equity in countries with efficient legal systems and stringent disclosure requirements. However, the cost of debt is strongly influenced by the quality of corporate governance in a poor regulatory and disclosure requirements regime.

Several studies in the literature confirm a negative relationship between the practice of good corporate governance and the cost of corporate capital (Art & Kim, 2005; Ashbaugh et al., 2004; Chen et al., 2003; Javaid et al., 2021; Thesarani, 2017). Furthermore, other researchers suggested that the practice of good corporate governance can reduce the asymmetry of information arising from agency problems through better disclosure practices and effective monitoring mechanisms, which can reduce agency costs and capital costs, especially the cost of equity. Therefore, based on the arguments of agency theory discussed above, the following hypothesis is put forward.

H_2: Corporate governance negatively affects the cost of capital of the company.

The Effect Costs of Capital on Profitability

The cost of capital is the rate of return required by a company to supply capital to finance an investment project by purchasing various securities. The concept of capital costs states that the optimal capital structure is a capital structure that can minimize the use of weight weight cost of capital. For the investor's point of view, all investors want the capital invested in the company to be able to obtain the maximum return. Shadab & Sattar, (2015)found evidence that there is a significant effect of weighted average cost of capital (WACC) on return on assets (ROA) using data of companies listed on the KSE 100 Index. Sharma, (2012) examined the effect of the cost of capital on profitability with industries in India sampled. The presence of a negative relationship between the cost of capital and profitability. With the increase in the cost of capital, the company's profit will automatically fall.

In line with Pertiwi & Darmayanti, (2018); Prastika & Candradewi, (2019). For the investor's point of view, all investors want the capital invested in the company to be able to obtain the maximum return. Otherwise, the investor will not be able to survive in the company. A company must maintain its profits and try to increase them. If the rate of return is not higher than the cost of capital, then an enterprise cannot survive and investors will turn to another company where they can get the maximum profit. Therefore, this study proposes the following hypothesis.

H_3: The cost of capital negatively affects the profitability of the company

The effect of capital costs in mediating corporate governance on company profitability

This research fills the research gap in the corporate financial literature by validating the existing relationship between corporate governance and profitability with the cost of capital as a mediator. In the literature explains that effective governance mechanisms can reduce information asymmetry and agency costs, capital costs and ultimately affect the performance of the company. Therefore, this study intends to investigate the impact of internal corporate governance mechanisms in generating profits by examining the role of capital costs in mediating corporate governance on profitability. A significant contribution of this paper is to discuss the influence of the quality of corporate governance on the achievement of maximum profits and capital costs in mediating the influence of corporate governance on profitability. So, based on this goal, the researcher proposed the following hypothesis:

H_4: The cost of capital can mediate the relationship between the attributes of corporate governance and the profitability of the company.

3. METHODS, DATA AND ANALYSIS

Research Variables and Operational Definitions

This study consists of three dependent variables, three independent variables and one mediation variable. The dependent variables in this study are Return On Asset (ROA), Return On Equity ROE) and Return On Investment (ROI), while the independent variables in this study are the size of the board of directors, the size of the board of commissioners and independent commissioners. In this study, the cost of capital was used as a mediating variable. Then ROE because it is generally used as the main indicator in the profitability ratio, when the ROE value is good, it will be followed by other profitability ratios (Lie, 2017). Furthermore, Return on Investment (ROI) because it describes the company's ability to invest all actively to make a profit.

The definition of each of these variables is as follows:

Return on Asset (ROA)

Return on assets is equal to net profit after tax divided by the total assets of the company. This ratio reflects whether the company uses assets effectively to generate its revenue, so this ratio is one of the important profitability indicators (Emmanuel & Riman, 2012).

ROA = (Net Profit After Tax)/(Total Assets) x 100%

Return on Equity (ROE)

Return on equity is equal to net profit after tax divided by shareholders' equity of the company. This ratio is a measure that shows investors how much profit a company can make, using the money invested from its shareholders (Zabri et al., 2016).

ROE = (Net Profit After Tax)/(Total Equity) x 100%

Return on Investment (ROI)
Return on investment is equal to profit after tax divided by the total assets of the company. One of the profitability ratios that measures the company's ability with all funds invested in assets for operating activities to get benefits (Maulita & Arifin, 2018).

ROE = (Net Profit Before Interest and Taxes)/(Total Capital) x 100%

Board of Directors (B_Size)
The board of directors has a vital role in the company, the increasing distribution of board members will cause more conflicts, but it can also provide alternatives to solving diverse problems than homogeneous board members (Pasaribu & Simatupang, 2019).

B_Size = Σ Board of Directors

Board of Commissioners (B_Com)
Judging from the large number of members of the board of commissioners, it is used as a measure of the board of commissioners in research (Frumentius & Christiawan, 2020). The board of commissioners is headed by a president commissioner or president commissioner.

B_Com = Σ of the Board of Commissioners

Independent Commissioner (Indp_Com)
Measuring an independent board of commissioners is carried out by dividing the number of commissioners by the total board of commissioners. More independent members in the board of commissioners tend to provide better oversight of management policies to improve company performance (Chabachib et al., 2020).

Indp_Com = (Independent Commissioner)/(Board of Commissioners)

Cost of Capital (Cost_Cap)
The cost of capital is the rate of return that the company must obtain from the invested projects. Referring to Ilyas, (2018), using weight average cost capital (WACC).

Cost_Cap = ((D x Rd) x (1-Tax) + (E x Re))

Information:
D = Cost of Capital
Rd = Cost of Debt
Tax = Tax Rate
E = Capital and Equity Levels
Re = Cost of Equity

Samples

The population in this study was all companies from various sectors listed on the Indonesia Stock Exchange during the research period. A total of 807 companies were made into populations, but not all populations were used as objects of research so sampling was needed. A sample is part of the number and characteristics possessed by the population (Sugiyono, 2013). The sampling technique used is the purposive sampling method, where the selection of sample members is based on predetermined criteria. The criteria used in this study are as follows:

1. Companies listed on the Indonesia Stock Exchange during the research period, namely from 2016 to 2020
2. Entire company with various sectors for generalization of research
3. Companies that publish annual reports consistently during the research period

4. Information contained in annual reports or financial statements that include all variables used in research

Based on the above criteria, there are 300 companies that are used as research samples, with the following details:

Table 1. Research Samples

No	Information	Total
1	All sectors of companies listed on the Indonesia Stock Exchange	807
2	Companies that do not publish consecutive annual reports or financial reports during the research year	65
3	Companies that do not have complete data for variable measurements	376
4	Eligible companies are used as research samples	366
5	Data *outlier*	66
	Total research data	300

This study was panel data that combined time series data with cross sections. with a structural equation model analysis method (Structural Equation Modelling / SEM) based on the Partial Least Square (PLS) variant using the SmartPLS statistical tool version 3.3.7. This study used path analysis with the following model:

$$Y = a + \beta_1 B\_Size + \beta_2 B\_Com + \beta_3 Indp\_Com + \beta_4 Cost\_Cap + \varepsilon 1$$

Description:
Y = Profitability
B_Size = Size of the Board of Directors
B_Com = Size of the Board of Commissioner
Indp_Com = Board of Independent Commissioner
Cost_Cap = The Cost of Capital of the Company as Measured by Weight Average Cost Capital (WACC)
α = Constanta
β1-4 = Beta Coefficient Regression
ε = Standard Error

4. RESULTS

Descriptive statistics describe the observation data used in the study including the amount of data (N), minimum value, maximum value, average value of the sample, as well as standard deviations from dependent variables, namely ROA, ROE, ROI and independent variables, namely the size of the board of directors, the size of the board of commissioners and independent commissioners. The cost of capital as a mediating variable in companies of all sectors listed on the Indonesia Stock Exchange in the research period from 2015 to 2020.

Table 1. Descriptive Statistics

Variable	N	Maximum	Minimum	*Mean*	Standard Deviation
ROA	1800	63.000	-156.000	1.681	10.651
ROE	1800	256.000	-1801.000	3.196	55.556
ROI	1800	1378.000	-1315.000	8.016	310.621
B_Size	1800	16.000	0.000	4.544	1.905
B_Com	1800	13.000	1.000	4.006	1.810
Indp_Com	1800	7.000	0.000	1.566	0.816
Cost_Cap	1800	50565.000	13133.000	34.349	1245.447

Source: Data processing SmartPLS

This study uses path analysis with SmartPLS software where the hypothesis results can be seen in Table 2 and Figure 2 as follows:

Table 2. Hypothesis Testing Results

	Original Sample	Sample Mean	Standard Deviation	T Statistic
Corporate Governance -> Profitability	0.029	0.049	0.025	0.087*
Corporate Governance -> Cost of Capital	0.033	0.034	0.015	2.130*
Cost of Capital -> Profitability	0.975	0.838	0.255	3.830*
Corporate Governance -> Cost of Capital -> Profitability	0.032	0.031	0.015	2.148*

* Significance 5%
Source: Data processing SmartPLS

Here are the results of hypothesis testing if presented in the form of a path analysis:

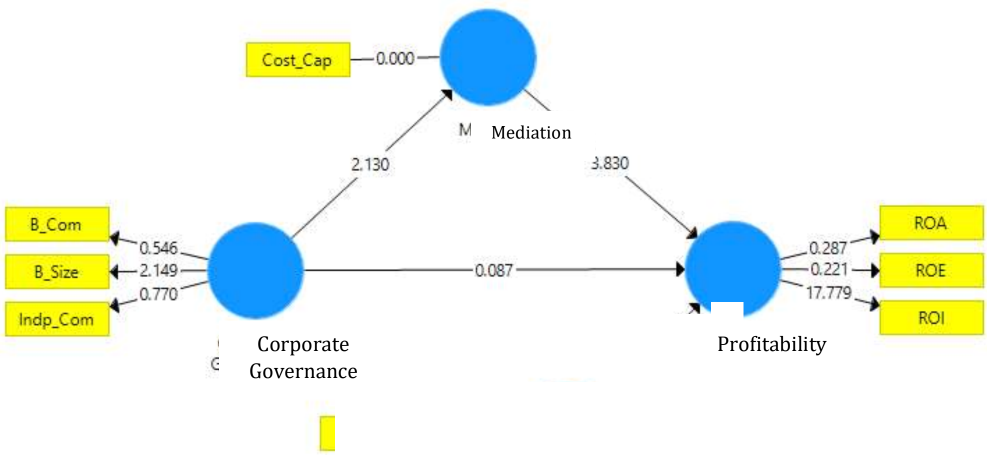


Figure 2. Hypothesis Testing Results
Source: Data processing SmartPLS

Based on figure 2, it can be seen that the dominant corporate governance attribute is the size of the company's board of directors (B_Size) with a value of 2,149, it illustrates that in corporate governance the board of directors is an important component, where the task of the board of directors is to manage the company in order to achieve goals. Then for the profitability variable, return on investment (ROI) which is the most dominant among the three profitability ratios, which is 17,779, it illustrates that in generating company profits, more is sourced from the return on investment from all company funds, both capital loans and own capital.

Based on statistical calculations, it can be concluded that the latent independent variable of corporate governance consisting of the size of the board of directors, the size of the board of commissioners and independent commissioners has an insignificant positive effect on the profitability of the company as measured by ROA, ROE and ROI. Where the t-statistic value of 0.087 < t of table 1.96, so **hypothesis 1 is accepted** (Ghozali, 2014). The results of the positive but insignificant research show that the relationship between corporate governance is directly proportional to the company's profit. When corporate governance is implemented properly, the company's profit will increase, but the large number of boards of directors in corporate governance cannot affect the company's return on investment (ROI). The results of this study are supported by the results of Habib, (2016) research argues that there should not be too many members of the board of directors, because a larger number contributes negatively to the company's performance.

The latent variables of independent corporate governance (the size of the board of directors, the size of the board of commissioners and independent commissioners) have a positive and significant effect on the cost of capital of the company as measured by the Weight Average Cost of Capital (WACC). Where the t-statistic value of 2,130 > t of table 1.96, so **hypothesis 2 is rejected** (Ghozali, 2014). Reducing the level of information asymmetry between investors and managers, then the cost of capital is reduced. Good governance practices can reduce information asymmetry, arising from agency issues, through better disclosure practices and effective monitoring mechanisms and therefore reduce agency costs and capital costs, in particular, the cost of equity. The results of this study are in line with (Botosan, 1997; Botosan & Plumlee, 2002).

The variable cost of capital has a positive and significant effect on a company's profitability as measured by ROA, ROE and ROI. Where the t-statistical value of 3,830 > t of table 1.96, so **hypothesis 3 is rejected** (Ghozali, 2014). Such results show that if the company's financing through debt and share capital increases, the profits resulting from the use of assets increase. This indicates the transfer of several sources of financing from the company under study in the form of assets. In addition, with the increase in the cost of capital, the return on equity also increases. The results of this study are in line with (Pouraghajan et al., 2012). Not in line with research Prastika & Candradewi, (2019); Shadab & Sattar, (2015) resulted in that the cost of capital with weight average cost of capital (WACC) has a negative and significant effect on profitability.

Based on the output from statistical calculations, it is concluded that there is a role of capital costs as mediation between the relationship of independent latent variables of corporate governance (the size of the board of directors, the size of the board of commissioners and independent commissioners) and profitability (ROA, ROE and ROI). Where the t-statistic value of 2,148 > t of table 1.96, so **hypothesis 4 is accepted** (Ghozali, 2014). It is proven in hypothesis 1 testing where the corporate governance variable does not have a significant effect on profitability. After measuring mediation with the role of variable costs of capital, corporate governance has a positive and significant effect on profitability. When the board of directors makes optimal capital structure decisions using weighted average costs of capital and the share capital increases then the profit from the return on assets, equity will increase.

5. DISCUSSION

The Effect of Corporate Governance on Profitability

In agency theory, the board of directors as an agent plays a role in determining the resource strategy and the direction of company policies both short and long term. The results of this study support agency theory where wise strategies and policies in decision making will improve the company's performance and effectiveness and have an impact on increasing company profitability. The greater the number of boards of directors in a company, the greater the profitability, so there is a positive relationship between the board of directors and profitability. This interpretation is supported by the results of this study where corporate governance (the more dominant board of directors) has a positive relationship with profitability, in line with the research of Hardiyawan et al., (2015). Any increase in the number of the board of directors will increase profitability, especially on the return on the company's investment returns. With the implementation of good corporate governance, it will improve the company's performance.

The Board of Commissioners as one of the good corporate governance mechanisms has the responsibility of supervising the financial reporting process and the quality of corporate governance. A high number of boards can improve supervisory functions and reduce agency conflicts that occur between agents and principals. In line with Mai, (2015) which states that the board of commissioners is able to increase the company's profit. The proportion of independent boards of commissioners in large companies is expected to contribute effectively in making a profit. The proportion of the board of commissioners in large companies is expected to contribute effectively in making a profit. However, this large proportion cannot increase profits, it is alleged that the proportion of independent commissioners of the company usually tends to be smaller than the proportion of its board of commissioners so that the arguments of independent commissioners do not have much influence on decision making.

The Effect of Corporate Governance on Costs of Capital

In carrying out supervision and control on the company's operations that are less effective, it will cause the determination of the company's funding or capital mechanism to be determined more by the board of directors. So it can be concluded that the greater the number of the board of directors, the higher the cost of capital of a company due to ineffective supervision. The results of positive influences are contrary to the initial hypothesis in this study which suspected the negative influence of corporate governance on the cost of company capital. These different results can occur because in public companies, investors tend to see the supervisory function carried out by the board of commissioners as less effective. This study does not support the research of Javaid et al., (2021); Thesarani, (2017)which provides evidence of a significant negative relationship between corporate governance and the cost of capital for companies through their direct impact on the decline of voluntary disclosure practices.

The Effect of Capital Costs on Profitability

Based on the results of the study, there is a unidirectional relationship between the cost of capital and the company's rate of return, which has a positive and significant relationship. If the financing of the company through debt and share capital increases, the profit resulting from the use of assets increases. This indicates the transfer of several sources of financing from the company under study in the form of assets. In addition, with the increase in the cost of capital, the return on equity also increases.The results of this study do not support the trade off theory, where the optimal capital structure is a capital structure that can minimize the cost of using overall capital or the average cost of capital so as to maximize profits. However, in line with Pouraghajan et al., (2012)which resulted in that changes in the value of the company's cost of capital had an impact on the company's ability to generate profits or profits.

The effect of capital costs in mediating corporate governance on company profitability

It is proven in hypothesis 1 testing where the corporate governance variable does not have a significant effect on profitability. After measuring mediation with the role of variable costs of capital, corporate governance has a positive and significant effect on profitability. The results of this study support the state that the more investors who invest in the company, the company's profits also increase. However, this is also inseparable from the performance of the company's management in managing funds from investors.

6. CONCLUSIONS, LIMITATIONS AND SUGGESTIONS

Conclusion

1. The research model proved to be feasible to use, evidenced by the results of goodness of fit with a value of R-Square > 0, which is 0.950 so that the model is said to be predictively relevant.
2. The results showed that corporate governance has a positive but not significant correlation to profitability. This is evidenced by the original sample value of 0.029 with a t-statistic of 0.087. It can be concluded that when implementing good corporate governance, the company's profitability also increases.
3. The results showed a positive and significant influence between corporate governance and the cost of capital. Evidenced by the original sample value of 0.033 with a t-statistic of 2.130. it can be concluded that good governance practices can reduce information asymmetry, by reducing the level of information asymmetry between insiders and outsiders of the company, it can lower the cost of capital.
4. The results showed a positive and significant influence between the cost of capital and profitability. This is evidenced by the original sample value of 0.975 with a t-statistic of 3.830. So it can be concluded that when the cost of capital increases, the company's expected rate of return also increases.
5. The results showed the role of capital costs as mediation in the positive and significant relationship between corporate governance and profitability. This is evidenced by the original sample value of 0.032 with a t-statistic of 2.148. This means that the implementation of corporate governance by increasing the cost of capital, profitability also increases.

Limitations and Suggestions

Researchers realize that the results of this study still have shortcomings. Where in the independent variable indicator there is still a loading factor whose value < 0.70 which affects the results of the Average Variance Extracted (AVE) so that the indicator must be reviewed or eliminated to produce an AVE value that meets the criteria. Further research should use other corporate governance component variables such as ownership structures, both institutional ownership, managerial ownership and others.

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