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RISK DISCLOSURE AND DEBT POLICY AS VALUE DETERMINANTS OF SMALL AND MID-CAP FIRMS[2]

The firm has to figure out how to fulfil shareholder prosperity in an asymmetric information situation. Debt as a signal is expected to do so, but there is no consensus yet, and most of the studies only focused on large-cap firms, leaving small and medium-cap firms with a higher information gap. This study's aim is to gain a more comprehensive understanding of the firm value determinant under the situation. Risk disclosure is expected to be an effective way to increase firm value, as the predicted role of debt is to increase firm value despite the risk it creates. Using partial least square to 179 small mid-cap firms in the Indonesian Stock Exchange, this study proposes risk disclosure to mediate the relationship between debt and firm value. Risk disclosure mediates the effect of debt on firm value. Debt will effectively increase firm value as it is supported by risk disclosure because it raises the investor's expectations. This result suggested that small mid-cap firms provide adequate risk disclosure so that debt utilization could effectively increase the firm value.
Keywords: risk disclosure; debt; firm value; asymmetry information; signaling; risk management; small mid-cap
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1. Introduction

A firm's value is determined by the different procedures it has gone through since its establishment. This value is crucial for the firm's long-term sustainability, including its current performance and prospects. A firm's share price reflects its value, affecting

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shareholder prosperity. Firm value refers to shareholders' benefits from holding stocks (Rashid, 2008). The firm's value is reflected in its share price; the higher the share price, the higher the firm's value because a high value indicates high shareholder prosperity (Fama & French, 2008). When investors purchase stocks, they expect an increase in firm value as a benefit.

In a public firm, the managers and shareholders are two distinct entities with differing levels of ownership and control. This separation leads to a disparity in information access and creates asymmetric information, with managers having greater access to internal firm information than shareholders. There is an informational gap between internal and external parties. This asymmetry can cause differences between the actual value of the firm and the value perceived by shareholders.

In this situation, managers will send signals to shareholders and investors. The signal could overcome the information gap and shape the outsider's perception of the firm's value. The tone of these signals also has a significant rule: a positive one creates a good impression on investors, increasing the firm's share price. Conversely, a negative one can cause a decrease in the firm's share price.

Debt is one of the most impactful financial decisions that can send a strong signal. Debt is one of the pivotal financial decisions that can effectively communicate a firm's financial standing and prospects. It signals lenders, creditors, and investors about firm creditworthiness, financial strength, and ability to repay obligations. Therefore, understanding the implications of debt and its impact on personal finance is crucial for making informed financial decisions. Debt represents a powerful signal of a firm's underlying value when the market lacks information symmetry (Howe, 1997). It is less sensitive to market information and provides a reliable means for firms to raise capital. Shareholders view debt as a firm promising prospects, and the future profits will not be shared with new shareholders, as opposed to equity funding sources (Brigham, 2019). This signal can increase the firm's value and raise its stock price.

Many empirical studies have shown that debt can significantly increase a firm's value. Firms should use as much debt as possible to achieve maximum firm value (Hansen, 1999). Companies can adjust their debt levels, set a goal, and gradually work to achieve it while increasing the desired firm value even if they exceed the industry average (Masulis, 1983; Cheng et al., 2010). Firm debt policy is crucial in determining a firm value as it significantly impacts investors' perceptions and expectations of its performance and prospects (Kalantonis et al., 2021). Elevated debt levels can lead to a firm value that is more excellent if carefully monitored to ensure proper allocation (Allayannis, Weston, 2001).

However, some other research results have been inconsistent because some scholars argue that there is a negative correlation between debt and firm value. If the debt is too high, the risk borne by the firm will also increase, and the goal of increasing firm value may not be achieved (Ruan et al., 2011; Fitria, 2016).

Most research in this field has been limited to firms with large capitalization or in specific industries. Nevertheless, there is a lack of empirical studies focusing on small and medium

capital firms. Small firms experience more significant asymmetric information problems and risks than larger firms (Huang et al., 2014),(Fama & French, 2008).

When a firm chooses debt as a financing option, it exposes itself to a higher level of risk, mainly if it is a small or mid-cap firm. While debt sends a positive signal to external parties, it may also have the opposite effect by lowering their expectations of the firm's value. Although more debt can lead to a higher expected rate of return, it also increases the risk that shareholders must bear (Brigham, 2019). Consequently, effective financial management is required to achieve the expected value and ensure long-term stability. To maximize a firm value, it is essential to proactively implement robust risk management strategies that effectively reduce overall risks (Fairchild, 2002).

An effective firm risk management strategy is crucial, and it should be proactively disclosed to external parties to demonstrate the firm's commitment to identifying and managing risks. Given the higher risks that smaller companies may pose, investors must obtain more comprehensive risk information (Fama & French, 2008). Small businesses can significantly enhance their value by proactively sharing risk disclosure with investors (Abdullah et al., 2015),(Miihkinen, 2013). In contemporary times, non-financial disclosures are increasingly recognized as a crucial reporting mechanism to effectively communicate a firm's dynamics. (Veysel, 2022). With the increasing emphasis on transparency and accountability in corporate governance, the issue of managerial and dominant owner discretion over information remains prevalent. However, this discretion can be effectively controlled by implementing high levels of corporate disclosure (Haj-Salem et al., 2020).

Scholarly research on corporate risk management disclosure primarily concentrates on the disclosure of enterprise risk management and its correlation with financial performance or firm value. Recent studies have examined the determinants of risk management disclosure (Goutami et al., 2022),(Restika & Lastiati, 2021), and (Anantha & Simatupang, 2022). Despite some inconsistencies in the results of various studies, there is evidence that risk disclosure impacts a firm's value. Furthermore, it is widely acknowledged that the tone of such disclosures plays a significant role in determining their effect on firm value (Miihkinen, 2013), (Abdullah et al., 2015), (Kamaruzaman et al., 2019), (Wahh et al., 2021), and (Abdullah Al-Dubai & M Abdelhalim, 2021).

The firm listed on the Indonesian Stock Exchange (IDX) must disclose its risk management details in the narrative section of its annual financial reports. This comprehensive risk management information disclosure enables firms to comply with regulatory requirements and helps bridge the information asymmetry between management and shareholders (Miihkinen, 2013). Sharing pertinent information is crucial to maintain market participants' favourable perception of a firm's value. By disclosing comprehensive information on risk management, firms can offer an insight into the risks they encounter and how they effectively manage them. Such transparent disclosure of information is essential in reinstating investor confidence in the firm's potential to appreciate its value and alleviate any apprehensions arising from using debt.

External funding can be acquired in various ways, and debt is often the preferred option due to its low cost and relative insensitivity to information. However, taking on debt also involves additional risks that can decrease market expectations about this strategy's effectiveness in

enhancing the firm value. It is essential to disclose the risks to investors to alleviate these concerns. This can ensure that their expectations of the firm's value are maintained. It is recommended that firms provide comprehensive information about risk management to ensure that investors are fully informed about the risks they may encounter and the actions to mitigate them. Transparency is the key to reinstating investor confidence and reigniting expectations of firm value growth, even amidst debt-related concerns. In summary, adequate risk disclosure can reinforce a firm's perceived value and support the positive impact of debt on its overall firm value.

This study was conducted to address inconsistencies found in previous research regarding the impact of debt on firm value as a signal. Most studies have focused on large companies, leaving small and medium-sized firms with a higher information gap. A study suggests utilizing risk disclosure as a connection to address a research gap regarding the relationship between a firm's debt and value. This study aims to achieve a more comprehensive understanding of this relationship. Risk disclosure is expected to be an effective way to increase firm value, as the predicted role of debt is to increase firm value despite the risk it creates. The findings of this study are expected to provide valuable insights into the financial landscape of the Indonesian Capital Market and help investors make informed decisions while investing in these firms.

This study investigates the role of risk disclosure in small and medium-cap firms listed on the Indonesia stock exchange. Specifically, the study will focus on four objectives:

1. To examine how an increase in debt impacts a firm's value.
2. To determine how an increase in debt affects risk disclosure.
3. To analyze how risk disclosure affects a firm's value.
4. To ascertain whether risk disclosure plays an intervening role in the effect of debt on firm value.

2. Small mid-cap firm profile in the Indonesian Stock Exchange

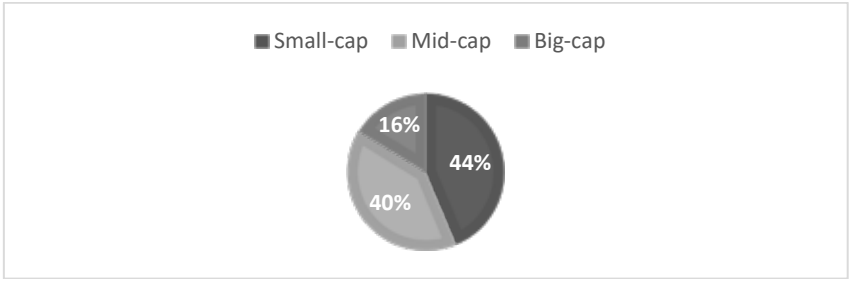
Small and medium-sized enterprises, in general, have an essential role in economic growth. Small and medium-sized enterprises generate employment opportunities and contribute to sustained economic growth in all nations (Kokeyeva et al., 2022). Although this is not clearly stated in a stock exchange community in a country, small and medium-sized firms certainly have an essential role as well. Its role is to develop its industrial sector and the stock exchange and balance trading on the stock exchange. On the Indonesia Stock Exchange (IDX), the trading volume of small and medium-sized firms does not experience the same growth as large firms. If we look at the number of small mid-cap firms on the stock exchange, they should have a significant role in the development and growth of the stock exchange and the economy. The following figure below is an overview of the proportion of firms on the IDX based on their capitalization in a pie chart.

Figure 1 shows that the most significant number of small capitalization firms on the IDX is 44% of all listed firms. At the same time, mid-capitalization firms account for only 16%. The

number of big capitalization firms in IDX is 40%. If you look carefully, the number of big-cap firms is lower than that of small-cap firms. Especially if we talk about the small mid-cap, the amount, if totalled, is 60% of all firms listed on IDX.

Research on various topics tends to emphasize big-cap firms, as their problem-solving abilities take centre stage on the stock exchange. While small mid-cap companies play a significant role, they present different risk characteristics than their larger counterparts.

Figure 1. Firm Capitalization Proportion in IDX



Source: author compilation

Nevertheless, the issues that small mid-cap firms must overcome are not much different than those big-cap firms face. As such, it is worthwhile to have more discussions on the same topic as large-cap firms but with a focus on their unique risk profiles.

3. Literature Review

Evaluating a firm's performance by its shareholders is a crucial factor in determining the business's success. This assessment is a key metric for measuring the firm's financial health and overall effectiveness in achieving its objectives. In business, shareholders hold a significant stake in a firm's success. If they feel the firm is not meeting their expectations, they may withdraw their investments and allocate them to other firms. This act of divestment could lead to a decline in the firm's share price, which can significantly impact the firm's overall performance and reputation in the market. To ensure the success of their business, managers must make it their top priority to generate value for their shareholders. This means they need to consider the expectations and interests of these shareholders, who have invested their money into the firm to receive benefits and profits. By prioritizing the needs of shareholders, managers can help build a more substantial and sustainable business that can thrive in today's competitive and fast-paced market.

Equity value is also known as shareholder value, while firm value includes equity and debt. According to Rappaport, shareholder value is the difference between corporate value and debt (Alfred Rappaport, 1998). Overall, the concept of shareholder value emphasizes the importance of considering the interests of shareholders when making decisions. By prioritizing shareholder value, firms can create a strong foundation for success and maintain the confidence of their shareholders.

Dalborg explains that value is created when the dividends and share prices exceed the costs of purchasing the shares (Fiordelesi, 2019). Shareholders benefit when the return on investment exceeds the costs incurred. To ensure the prosperity of shareholders, managers have to maximize the present value of all anticipated future shareholder earnings (Ross, Stephen A, Waterfield, Randolf A, Jaffe, Jeffry F, Robert, 2015). It is a commonly held notion that shareholders are primarily interested in the stock market's performance and the price fluctuations of their shares.

Serven defines shareholder value as the market value of a firm ordinary shares. A firm's valuation is denoted by its share price, implying that a higher share price indicates a greater firm value. This, in turn, leads to increased prosperity for its shareholders. The outcome of this phenomenon is that firms can enhance their market value and create value for their stakeholders. The value of a firm is dependent on its performance and growth throughout its history, making it essential to optimize its sustainability for future success (Eccles et al., 2014). Measuring a firm value is necessary to convey its current wealth and future investment prospects with the utmost clarity (Rau, 2016).

Signalling theory is a crucial concept in information economics that aims to explain how two parties with unequal access to information can effectively communicate through signals. This theory is particularly relevant when one party possesses more information than the other, which can lead to adverse selection or moral hazard problems. By sending signals, the informed party can convey valuable information to the uninformed party, thereby reducing the information asymmetry and improving the market's overall efficiency. It is a powerful tool for bridging the gap between parties with divergent levels of information (Connelly et al., 2011).

In the business world, there exists a distinction between the shareholder, who owns the firm, and the manager, who is responsible for its management. Shareholders entrust managers with the task of increasing the firm's market value. It is common for firms to maintain confidentiality around their strategies to stay competitive. However, it is essential to balance confidentiality and transparency to ensure accurate information is disseminated. Sometimes, a lack of transparency can lead to misunderstandings or incorrect assumptions.

When a firm decides to go public, the value determined in the process may not always accurately reflect its true worth. This can occur due to incomplete disclosure of information by the firm's management. In such cases, investors may end up paying a price that does not align with the firm's value. In this state, investors face a challenge in distinguishing between firms of varying qualities because both good and bad firms can emulate market signals. This can make it difficult for investors to make informed investment decisions and can potentially lead to undesired outcomes. To establish a unique position in the market, firms must convey distinctive signals that differentiate them from their competitors, particularly those offering inferior products or services. However, this task is not a straightforward one and demands a high degree of complexity and substantial costs that only high-quality firms can afford to bear. A firm can use two types of signals to display its credibility and longevity to the market: debt as a source of financing and distributing dividends (Core, 2001).

When a business is looking for investors or partners, the amount of debt it carries can be a valuable indicator of its actual value. This is especially true when there is unequal access to

information between the business and the potential investors or partners. Essentially, debt can signal a business's financial stability and potential to those interested in working with it. Many firms continue to distribute dividends and use debt to signal their excellent credibility and longevity (Howe, 1997). changes in the firm's capital structure significantly impact its value (Bui & Nguyen, 2023).

Businesses often prefer financing their operations through debt instruments rather than equity when they anticipate a high likelihood of profitability. This is because issuing equity can be perceived as unfavourable and can signal a negative impression, as it may convey that the firm's capacity to generate profits has reduced compared to its previous performance. In some situations, introducing new shares by a firm can indicate that the firm's current share price is overvalued. This could be because the firm is attempting to raise more capital by selling additional shares, which can dilute the value of existing shares held by shareholders. As a result, investors may interpret the decision to issue new shares as a negative signal about the firm's financial health and prospects. There is a common belief that acquiring additional debt is a favourable development, which sends a positive signal to the financial market. On the other hand, releasing more shares is typically perceived as unfavourable news, delivering a negative message in the market.

In 2001, Charles conducted a study that defined risk in finance as an unforeseen outcome or when the results differed from what was expected (Tapiero, 2004). Although risks are commonly perceived as something negative that could lead to unfavourable consequences, it is crucial to recognize that venturing into the unknown can also present opportunities for growth and advancement. Taking calculated risks can catalyze innovation, learning, and progress in personal and professional contexts. Therefore, it is essential to approach risk-taking with a balanced mindset, weighing the potential benefits and drawbacks before deciding. Effectively managing risks is a fundamental aspect of strategic planning for companies seeking to achieve their desired outcomes in the future. This entails deliberately balancing the potential losses and opportunities from risk management. By skillfully navigating these intricacies, businesses can position themselves for long-term success.

Risk management is a crucial process that helps firms identify, assess, and prioritize risks affecting their operations, assets, or reputation. The firm can ensure survival, improve resilience, and optimize opportunities by effectively managing risks. This involves implementing strategies, policies, and procedures that minimize the likelihood of risks occurring and mitigating their impact in case of occurrence. Ultimately, risk management is an ongoing effort that requires continuous monitoring, evaluation, and improvement to ensure a firm is prepared to face any challenge.

Corporate risk management is a strategic and all-encompassing process that involves identifying, analyzing, and evaluating potential business risks. It is a systemic approach focusing on a firm's comprehensive risk management system. The risk management process involves identifying and assessing the magnitude and possible impact of risks the firm encounters. It also includes evaluating the feasibility of methodologies to mitigate, manage, transfer, or avoid risks (Kloman, 1992). It aims to develop a proactive and systemic approach focusing on a firm's overall risk management system, including policies, procedures, and practices. The objective is to prevent any potential losses that may result from the exposure to various risks faced by the business, such as financial, operational, legal, or reputational

risks. By implementing a robust risk management system, a firm can safeguard its assets, reputation, and sustainability in the long run.

To effectively create and maintain value, the firm must adhere to value management principles, which require a deep understanding of the interaction between costs, risks, and benefits (Heinle & Smith, 2017). When a firm aims to enhance its value by making strategic decisions, it needs to have a sharp perception of the potential risks involved while considering the anticipated benefits. This requires a comprehensive assessment of the risks associated with the decision and a careful analysis of how the expected benefits can outweigh those risks. A thorough evaluation of risks and benefits is crucial in making sound strategic decisions to help the firm achieve its goals and create long-term value.

In the interest of protecting shareholder value, firms must adopt a proactive approach to risk management. This entails the identification of potential threats and uncertainties that may pose a risk to the business and the implementation of measures to either mitigate or eliminate them while ensuring that the firm's overall objectives and goals are being met. By taking a proactive stance towards risk management, firms can safeguard the financial interests of their shareholders and foster trust and confidence among stakeholders. Hence, risk management is an integral component of effective corporate governance, and firms must prioritize formulating and implementing robust risk management frameworks to ensure long-term success and sustainability.

Since traditional financial disclosures do not include intangible assets, stakeholders have expressed concern about voluntarily disclosing information about their non-physical assets to analyze firm performance and future growth pathways more accurately (Singhal et al., 2022). Making informed investment decisions depends on understanding the potential risks associated with a particular firm. Therefore, providing detailed information about the firm's risk management can significantly aid investors' decision-making.

Risk disclosure is a pivotal process that facilitates firms in providing investors and other stakeholders with comprehensive information regarding the risks they are exposed to and the measures being taken to mitigate them. This process ensures transparency, accountability, and informed decision-making by all parties involved. Disclosing potential risks and the actions being taken to address them is a regulatory requirement and a fundamental aspect of corporate governance. It helps foster trust and confidence among stakeholders and enhances the firm's credibility. Hence, risk disclosure should be considered an integral part of a firm's overall risk management strategy. Incorporating this practice can significantly contribute to building a transparent and accountable organizational culture. Moreover, this approach would offer valuable insights to external stakeholders about the firm's comprehensive risk management strategy, further enhancing its credibility and reputation in the market.

Publicly traded firms in most countries are required to disclose their risk management practices to a regulatory agency. This agency oversees and regulates the process of disclosing such practices to ensure transparency and accountability in the management of risks by these firms. As per the regulatory framework of the Indonesia Stock Exchange (IDX), public companies must disclose their risk management strategies in the narrative section of their annual financial reports. The IDX mandates reporting four types of risks as part of the

enterprise risk management framework, and an additional risk report is voluntary. Mandatory risk requires reporting on three types of risk: credit risk, liquidity risk, and market risk.

Enterprise risk management involves three types of risks, integral to how companies handle their finances. However, companies should provide more disclosure than necessary to address limitations in general risk disclosure. This extra disclosure is known as voluntary risk disclosure. According to (Abdullah et al., 2015), voluntary risk disclosure can impact a firm's value, while Miihkinen has suggested that companies with solid risk disclosure can reduce information asymmetry between managers and shareholders (Miihkinen, 2013). Adequate disclosure of risk information can also prevent a decline in market expectations of a firm's value. By providing transparent information about risk management, companies can offer an overview of the risks they face and how they manage them, ultimately restoring confidence in their value and mitigating debt-related concerns.

Based on previous research and theories, it has been suggested that debt can be a driving force for a firm to increase its value (Allayannis & Weston, 2001). According to this view, incorporating higher debt levels can encourage firms to allocate and manage resources more responsibly, leading to better financial outcomes. A higher debt level can also be a positive signal to potential investors, demonstrating the firm's strong performance and promising prospects. Positive signals can increase the firm's stock price (Michelon & Parbonetti, 2012). The firm debt policy can communicate its performance and prospects to external parties, ultimately affecting its value (Kalantonis et al., 2021). Strategic use of debt can be a powerful tool for a firm to enhance the financial well-being of its shareholders while also boosting its overall value. The careful management of debt can profoundly impact how investors perceive the firm and their expectations for its future growth potential. This underscores the crucial role that positive signals play in driving value creation for businesses -the first hypotheses in this study are as follows.

H1: A higher debt effect will increase firm value

The prudent use of corporate debt is a crucial consideration to achieve higher expected returns while minimizing shareholder risk exposure (Hansen, 1999). Smaller firms, in particular, are perceived as higher-risk entities, thus requiring greater information disclosure on potential risks to gratify investor requirements (Rashid, 2008). Firms that provide comprehensive risk information can effectively reduce information asymmetry between managers and shareholders, thereby enhancing shareholder value (Anantha & Simatupang, 2022). It is highly recommended that companies establish and implement reliable risk management procedures to efficiently identify, assess, and mitigate potential risks that could impact their business operations. Furthermore, companies should openly communicate their risk management strategies and practices to relevant stakeholders, including investors, regulators, and employees, to enhance transparency, build trust, and foster a culture of accountability and responsibility. Incorporating debt as a part of their financial strategy should encourage companies to improve their risk disclosure techniques, ensuring that they operate with transparency and accountability. This can help to create a more secure and stable financial system while also providing investors with the information they need to make informed decisions – the second hypothesis in this study is as follows.

H2: A higher debt effect will increase firm risk disclosure

In order to improve the overall value of a firm, it is imperative to manage accounting figures efficiently. This involves reducing variability and minimizing the risk of financial difficulties. By doing so, businesses can maintain a stable financial position, which helps them achieve long-term success. Managing risk is also essential to increase the firm value (Salem et al., 2019) and (Paxia & Suhendah, 2022). The effective management of risks is widely acknowledged as a crucial factor in enhancing the value of a firm. Firms can protect their assets, reputation, and sustainability by identifying, evaluating, and addressing potential risks. As such, risk management has emerged as a critical aspect of contemporary business strategy, with its importance increasingly recognized in academic literature and corporate practice. Therefore, firms must develop robust risk management frameworks that enable them to navigate the complexities of their operating environment and seize opportunities for sustainable growth. At the level of an investor, having a good understanding of the relationship between different entities can be valuable in predicting the potential risks associated with portfolio selection. By analyzing and gathering information on expected operational changes, investors can make informed decisions that can help mitigate potential risks and maximize returns. Recent research identified three key points. They are, firstly, disclosing the risk of increasing a firm stock price. Secondly, high-growth firm share prices respond asymmetrically to positive and negative risk disclosures (Tan et al., 2017). Lastly, only firms that generate profits are affected by positive and negative disclosures. However, corporate risk disclosure negatively impacts firm value, potentially due to the cost of preparing information exceeding the benefits obtained (Kamaruzaman et al., 2019). – the first hypotheses in this study are as follows – the third hypotheses in this study are as follows.

H3: Risk disclosure affects the firm value

Debt usage can signal a firm's real value in circumstances featuring asymmetric information (Howe, 1997). However, as a firm debt increases, so does the risk it encounters, thus posing a discouraging challenge for shareholders (Brigham, 2019). This is particularly true for small firms, which are more susceptible to risk than their larger counterparts (Fama & French, 2008). In order to tackle this obstacle effectively, investors are requesting a higher level of clarity and openness concerning the procedures and strategies employed for managing risks. This would enable them to make informed decisions and minimize uncertainties while investing. The importance of comprehensive disclosure of risk information is to reduce information asymmetry between managers and shareholders (Abdullah et al., 2015). To accurately reflect a firm's growth potential through its debt, it is vital to share comprehensive details about its risk management and mitigation strategies with external stakeholders. This is especially crucial when a firm has significant debt, as the associated risks can greatly impact its prospects. By disclosing this information, a firm can enable external stakeholders to make informed decisions regarding their investments and uphold their trust in the firm's capability to manage its debt prudently. The involvement of intermediaries enables the disclosure of potential risks that come with borrowing and improves the efficiency of debt utilization. These intermediaries bridge the borrowers and lenders, providing valuable

insights and guidance to both parties. Doing so helps minimize the possibility of default and ensures that the funds are utilized effectively, ultimately contributing to the economy's growth. The fourth hypothesis in this study is as follows:

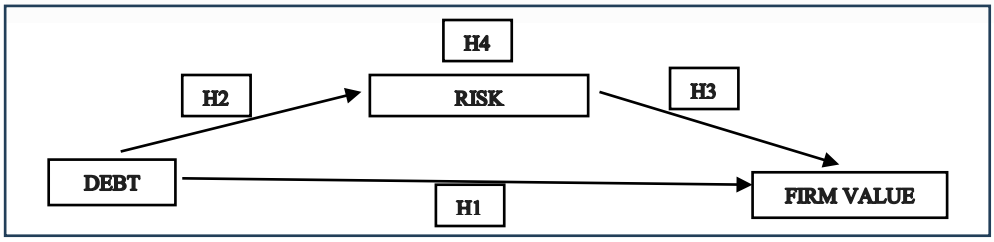
H4: Risk disclosure mediates the debt effect on firm value

4. Research Methodology

The research conducted an in-depth analysis of 179 small to medium-sized companies operating in the Indonesian Capital Market, spanning various industries. The study was carried out over four years, from 2018 to 2022, to comprehensively understand these firms' market trends and performance. To qualify for the study, a firm market value must fall between 1 trillion and 50 trillion Indonesian rupiah, which is required for admission into the small to mid-cap IDX index.

The present study examined the associations among the firm's value, debt level, and risk disclosure. Debt was considered an independent variable, risk disclosure acted as a mediator, and firm value was the dependent variable. The research findings demonstrated the presence of interrelationships among these variables. Firm value measurement uses Tobins Q, which is the ratio between the sum of total market value and total book value of liabilities compared to the total book value of assets (Adam &(Adam & Goyal, 2008). the debt uses Debt to Equity Ratio$_{t-1}$, which compares total debt to equity (Allayannis & Weston, 2001). The mediated variable risk disclosure is the index ratio t-1, which compares voluntary and mandatory risks (Abdullah et al., 2015). The IDX mandates reporting four types of risks as part of the enterprise risk management framework, and an additional risk report is voluntary. Four types of mandatory risk are interest rate risk, currency risk, credit risk, and liquidity risk.

Figure.2. Hypotheses Development



Source: author compilation

Figure 2 presents the direct causal effect of debt and risk disclosure on firm value and the immediate effect of debt on risk disclosure. It also shows the indirect effect of debt on firm value with risk disclosure as the mediated variable. Each arrow points to the direct impact (H1, H2, H3), and the indirect effect is between the direct effect of debt to risk disclosure and risk disclosure to firm value (H_4).

5. Result and discussion

The results of the statistic description are presented in Table 1 below. The description is divided into each variable with a description of average, standard deviation, minimum, and maximum.

Table 1. Descriptive Statistic

Variable	Number Observation	Average	Standard Deviation	Minimum	Maximum
Firm Value	179	1,069	1,138	0,01	5,5
Debt	179	0,599	0,831	0,01	8,88
Risk Disclosure	179	1,377	1,102	0,18	4,54

Source: author compilation.

The following is a summary of the descriptive statistics of the variables based on 179 observations, as presented in Table 1. The average firm value of 1.069 indicates that small mid-cap firms are valued more than their tangible assets. This suggests that investors are optimistic about the prospects of these firms. Additionally, the average debt of 0.599 suggests that most small mid-cap firms can grow and expand using debt without jeopardizing their shareholder wealth. This is a positive sign for these firms as it implies a healthy financial structure.

The risk factor for small mid-cap firms, as indicated by the average value of 1.102, shows that most firms disclose more voluntary risk than mandatory risk. This means they proactively identify and disclose risks to their investors, which is a good practice. The variables' standard deviation and maximum and minimum values indicate a relatively broad data distribution. This suggests a wide range of values for these variables, which may provide valuable insights for investors and analysts interested in understanding small mid-cap firms' financial performance and risk profile.

Table 2 shows the results of the outer model analysis by looking at its validity and reliability. Validity and reliability criteria can also be seen from each construct's composite reliability (CR) value and the Average Variance Extracted (AVE) value. The construct is highly reliable if the value is 0.70 and the AVE is above 0.50. The results of Composite Reliability and AVE values for all variables meet the criteria of discriminant validity. In addition, all Average Variance Extracted (AVE) values are> 0.50, and all Cronbach's Alpha (CA) values are> 0.70 so that all variables are reliable.

Table 2. Outer Model Measurement

Variable	CA	CR	AVE
Debt	1	1	1
Risk Disclosure	1	1	1
Firm Value	1	1	1

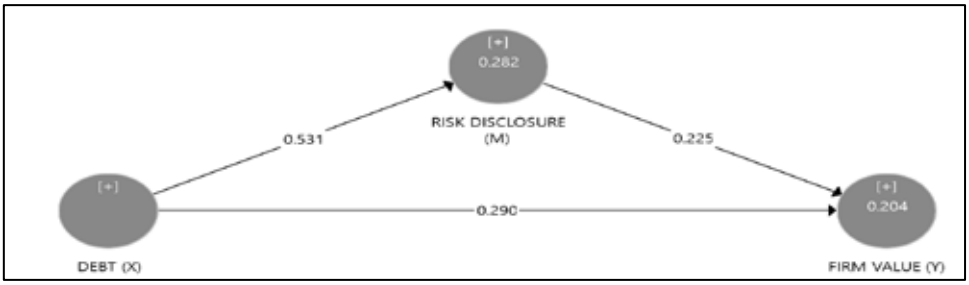
Source: Author's Primary Data Proceed.

The structural model is evaluated by considering the Q^2 predictive relevance model, which measures how well the model generates the observation values. Q^2 is based on the coefficient of determination of all dependent variables. The magnitude of Q^2 has a value with a range of $0 < Q^2 < 1$; the closer the value of 1 means, the better the model (Hair et al., 2017). The

results of the structural model evaluation obtained Q^2 of 0.428 the results of this test provide evidence that the goodness of fit of the structural model is good or prove that this model is considered to have good predictive relevance. In other words, it can be interpreted that the information contained in the data, 42.8%, can be explained by the model.

The inner or structural model is evaluated to test the relationship between the research model's variables, significance value, and R-square. Based on the statistical results such as significant value, R square value, and f-square value, the summary result is presented in Figure 2.

Figure 2. Structural Model



Source: author compilation.

The R-square estimation result using Smart PLS is displayed in the following table.

Table 3. R-Square Value

	R Square	R Square Adjusted
FIRM VALUE (Y)	0.204	0.202
RISK DISCLOSURE (M)	0.282	0.281

Source: author compilation.

The statistical analysis presented in Table 2 reveals that the risk disclosure (M) level is moderately influenced by the amount of debt (X), as indicated by an R-square value of 0.282. Specifically, this means that changes in debt levels can explain 28.2% of the variability in risk disclosure. Additionally, the analysis shows that the firm value (Y) is moderately influenced by risk disclosure and debt, with an R-square value of 0.204. This suggests that 20.4% of the variation in firm value can be attributed to changes in risk disclosure and debt levels.

To better understand the magnitude of influence between these variables, we can refer to effect size or f-square. Generally, a f-square value of 0.02 is considered small, 0.15 is medium, and 0.35 is large.

The results presented in Table 3 indicate that the magnitude of influence between the variables is moderate.

Table 4. f-Square value

	FIRM VALUE (Y)	RISK DISCLOSURE (M)
DEBT (X)	0.076	0.392
RISK DISCLOSURE (M)	0.046	

Source: author compilation.

The f-square values of debt significantly impact risk disclosure, with a debt f-square of 0.392 indicating a high influence on the risk disclosure. However, the f-square value of debt at 0.076 shows that it has a small effect on the firm's overall value. In comparison, the f-square value of risk disclosure is even smaller at 0.046, which indicates that it has a minimal effect on the firm's overall value. Therefore, it is essential to analyze the f-square values of debt and risk disclosure to accurately determine their impact on the firm's value.

The significance of the estimated parameters provides beneficial information regarding the relationship between variables. The results of hypothesis testing are as follows:

Table 5. Hypothesis Test

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values
DEBT (X) -> FIRM VALUE (Y)	0.290	0.288	0.061	4.725	0.000
DEBT (X) -> RISK DISCLOSURE (M)	0.531	0.530	0.042	12.598	0.000
RISK DISCLOSURE (M) -> FIRM VALUE (Y)	0.225	0.222	0.037	6.026	0.000

Source: author compilation.

The research study was analyzed to determine the impact of debt on firm value and risk disclosure. Table 4 presents the findings, which indicate a statistically significant direct effect of debt on firm value. The p-value for the effect of debt on risk firm value is lower than 0.05 (0.000), and the original sample estimate value is positive (0.290), which implies that the effect is positive. As a result, the first research hypothesis, which stated that debt significantly affects firm value, is accepted.

The study also found that debt has a significant direct effect on risk disclosure. The p-value for this effect is lower than 0.05 (0.000), and the original sample estimate value is positive (0.531), indicating that debt directly affects risk disclosure. Therefore, the second research hypothesis, which stated that debt significantly positively affects risk disclosure, is accepted.

Finally, the analysis revealed a statistically significant direct effect of risk disclosure on firm value. The p-value for this effect is lower than 0.05 (0.000), and the original sample estimate value is positive (0.225), meaning that risk disclosure positively affects firm value. Therefore, the third research hypothesis, which states that risk disclosure has a positive, significant direct effect on firm value, is accepted.

Table 6. Mediation Test

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (|O/STDEV|)	P Values
DEBT (X) -> RISK DISCLOSURE (M) -> FIRM VALUE (Y)	0.119	0.118	0.023	5.171	0.000

Source: author compilation.

The findings presented in Table 5 demonstrate that the amount of debt a firm holds has a noteworthy and positive influence on its value by disclosing risks. The statistical analysis reveals a p-value below the threshold of 0.05 (0.000), along with an original sample estimate value of 0.119, indicating a positive and significant indirect effect. Thus, it can be concluded that the fourth hypothesis of this study is accepted, which suggests that debt has a significant and positive indirect impact on the value of a firm through risk disclosure acting as a mediator.

The statistical analysis of the research data confirms that a firm's debt level has a significant and positive impact on its overall value and level of risk disclosure. Specifically, the study's results indicate that the original sample estimates for the effects of debt on risk firm value, risk disclosure on firm value, and debt on firm value through risk disclosure as a mediator are all positive. As a result, we can conclude that all the hypotheses proposed in this study are accepted. These findings provide valuable insights for businesses and investors, highlighting the importance of managing debt levels and balancing risk and value to optimize overall performance.

The findings of this study demonstrate a significant positive relationship between debt and risk disclosure, as well as a significant positive association between risk disclosure and firm value. The mediation analysis reveals a significant positive result that confirms the existence of complementary mediation, indicating the presence of omitted variables in the research model. This result can be classified as complementary mediation (Zhao et al., 2010), confirming the existence of omitted variables, which are not included in this research model. In addition to risk disclosure, other variables mediate the indirect effect of debt on firm value. These results suggest that debt plays a crucial role in shaping risk disclosure and, ultimately, firm value and that the relationship is complex, involving multiple mediating variables.

6. Conclusion

Scholars are constantly investigating the intricate relationship between debt and firm value. The issue of whether debt has a positive effect on firm value has been the subject of extensive academic research in finance and accounting. One school of thought suggests that an increase in debt can signal a firm's promising prospects and robust performance, which may be due to its ability to leverage its existing assets and generate greater returns. This signal can significantly contribute to boosting the firm value as it forms market perceptions and expectations of the firm, which are then reflected in its rising stock price. On the other hand, excessive debt can result in a decline in firm value, leading to financial distress and an

increased risk of default. Therefore, companies must maintain an optimal level of debt relative to their assets, cash flow, and overall financial health. This can help them maximize their value while minimizing risk and ensuring long-term sustainability.

Numerous academic studies have delved into the positive impact of debt on risk disclosure. According to research, firms with higher debt levels are more likely to disclose risk management information, which is especially crucial for small to mid-sized companies. External stakeholders, such as investors and creditors, require comprehensive information from the firms to reduce information asymmetry. This risk disclosure encompasses mandatory and voluntary disclosures, providing stakeholders with enough information to understand the firm's risk profile. In conclusion, the relationship between debt, firm value, and risk disclosure is intricate and requires a balanced and sustainable approach to financial management.

According to previous research, firms that provide a detailed and comprehensive overview of their risk management practices are more likely to experience an increase in their overall value. Risk management has been identified as a critical factor in enhancing the value of a firm (Fairchild, 2002). By disclosing comprehensive information related to their risk management practices, firms can send a signal to market participants, which can significantly influence their perceptions and expectations of the firm and ultimately increase its stock price (Tan et al., 2017). Therefore, firms must prioritize risk management practices and communicate their efforts to the market transparently and effectively.

When a firm takes on debt, it exposes itself to various risks that can affect its overall value. However, debt can also be a strategic funding decision that helps increase a firm's value by effectively managing risks. In order to make informed investment decisions, external parties such as investors require access to relevant information. This is particularly important for small to mid-cap companies with less information available than larger companies, resulting in information asymmetry. By providing comprehensive risk disclosures, companies can reduce this information asymmetry and provide investors with the necessary information to evaluate the risks associated with their investments.

Risk management and disclosure are essential for companies to increase their value in today's business environment. Implementing effective risk management practices and comprehensive disclosure of these practices can significantly improve market participants' perceptions and expectations of a firm. The disclosure of risk management practices can also reduce information asymmetry, which is particularly important for small and mid-cap companies with higher levels of information asymmetry. By providing necessary information for investors to evaluate the firm's risks, risk disclosure can help these companies reduce information asymmetry.

Moreover, effective risk management can increase a firm's value through debt. However, it is crucial to communicate associated risks to prevent negative perceptions and expectations from external parties. Effective risk management practices can help firms minimize the impact of adverse events, and comprehensive risk disclosure can help investors understand how the firm manages risks.

In conclusion, risk management and risk disclosure are critical for firms to achieve their business objectives and increase their value. By implementing effective risk management practices and disclosing them comprehensively, firms can improve their reputation, reduce information asymmetry, and enhance their debt value.

The results of this research show that there is a complementary mediation effect at play, which suggests that there may be an omitted variable influencing the indirect effect of debt on firm value. This finding provides an exciting opportunity for future research to investigate and identify this missing variable, which could serve as an intermediary in the relationship between debt and firm value. By uncovering this mediating variable, we can gain a more comprehensive understanding of how debt affects the value of a firm and potentially discover new ways to increase firm value. This research highlights the importance of considering all variables that may impact the relationship between debt and firm value and encourages researchers to continue exploring this area to uncover new insights and opportunities for growth.

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