

The Effect of Liquidity Management, Cost Structure, and Leverage Policy on Financial Performance in the Retail Sector in Jakarta

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ABSTRACT

This study examines the effect of liquidity management, cost structure, and leverage policy on the financial performance of retail sector companies in Jakarta. Utilizing a quantitative approach, primary data were collected from 165 respondents using a structured questionnaire measured on a Likert scale of 1-5. Structural Equation Modeling-Partial Least Squares (SEM-PLS 3) was employed to analyze the relationships between the independent variables—liquidity management, cost structure, and leverage policy—and the dependent variable, financial performance. The findings indicate that all three factors significantly and positively influence financial performance, with leverage policy showing the strongest effect. The study underscores the importance of strategic financial management practices for retail companies to enhance profitability and sustain competitive advantages. Practical implications include adopting efficient liquidity tools, optimizing cost structures, and strategically managing leverage to maximize growth and stability.

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1. INTRODUCTION

The retail sector in Jakarta significantly contributes to economic development but faces challenges requiring effective financial management strategies. Liquidity management is vital for meeting short-term obligations and maintaining operational stability, with the current ratio commonly used as a measure, although it alone does not significantly impact financial distress [1]. Decreasing liquidity ratios may indicate potential short-term financial issues, underscoring the importance of careful liquidity management [2]. Optimizing cost structures by managing expenses is essential

for improving profitability, with metrics like ROA and ROE often used to assess financial performance [2]. Additionally, the total asset turnover ratio significantly affects financial performance, emphasizing the need for efficient asset management [3]. Leverage policy, measured by ratios such as debt-to-equity and debt-to-asset, plays a critical role in financial performance; while leverage can enhance returns, it also increases financial risk [4]. Furthermore, the debt-to-asset ratio has a significant negative effect on financial distress, highlighting that high leverage can lead to financial instability [1].

Efficient liquidity management is essential for retail businesses with tight margins and high inventory turnover, ensuring short-term obligations are met and operational stability is maintained. Strategic financial practices are vital for balancing liquidity to prevent disruptions, as high profitability often aligns with low liquidity levels [5]. Effective liquidity management supports stable growth, profitability, and resilience against financial crises [6]. A positive link between liquidity and profitability is evident in Romanian retail firms and India's Powergrid, where adequate liquidity ensures smooth operations [7], [8]. Managing current assets and liabilities to maintain balanced liquidity is crucial, as excess or inadequate liquid resources harm performance [8]. Best practices, such as monitoring cash conversion cycles and aligning liquidity with investments, optimize financial outcomes [6].

Cost optimization in a competitive retail environment is essential for enhancing profitability, requiring effective management of both fixed and variable costs while maintaining quality and customer satisfaction to secure a competitive edge. Production costs, particularly in the food and beverage sector, significantly influence profits, with effective management of production, promotion, and sales expenses showing a 79.3% joint effect on profitability [9]. In industrial companies, understanding the cost structure, including fixed and variable costs, is critical for maximizing profitability through informed decisions that increase production and reduce unit costs [10]. The cost of quality (CoQ) is shaped by competitive strategies such as cost leadership, centralization, and formalization, which positively influence CoQ and highlight the importance of strategic alignment in optimizing quality-related expenses [11]. Identifying changes in cost structures over time, particularly the balance between fixed and variable costs, is vital for effective pricing and business efficiency [12]. Additionally, systematic control of cost determinants is crucial, as even minor adjustments can significantly impact

profitability, as demonstrated in a textile company case study [13].

Leverage policy, which involves using borrowed funds to finance operations, is a critical factor in shaping the financial performance of retail firms. While leverage can amplify profits during favorable economic conditions, it also introduces substantial risks, especially in volatile markets, making a balanced leverage policy essential for sustainable growth. Excessive debt can lead to financial distress, highlighting the need for careful management. Leverage significantly influences financial results by enhancing profits in positive economic climates but requires a thorough analysis of its impact on capital structure [14]. During financial crises, the relationship between liquidity, leverage, and business growth becomes more complex, necessitating effective risk management and diversified funding strategies [15]. Flexible and well-considered resource management is crucial, balancing the profit potential of borrowing against its risks [14]. Strategies such as improving operational efficiency and diversifying funding sources help ensure stability during financial challenges [15]. Firm size also plays a role, with larger companies better equipped to manage leverage effectively, potentially mitigating its adverse effects [16]. In some cases, leverage has limited impact on financial performance, suggesting that factors like liquidity may hold greater significance [16], [17].

Despite the importance of these factors, there is limited empirical evidence on how liquidity management, cost structure, and leverage policy collectively influence financial performance in the retail sector, particularly in Jakarta. Addressing this gap, this study seeks to provide insights into the financial strategies of retail companies and their impact on performance outcomes, with objectives that are threefold: 1) to assess the impact of liquidity management on the financial performance of retail companies in Jakarta, 2) to evaluate the influence of cost structure on financial performance in the

retail sector, and 3) to examine the effect of leverage policy on financial performance in retail businesses.

2. LITERATURE REVIEW

2.1 *Liquidity Management and Financial Performance*

Effective liquidity management is essential for retail companies to meet short-term obligations and maintain smooth operations by balancing asset conversion into cash and optimizing resource utilization. Liquidity management is crucial for ensuring solvency and profitability, enabling firms to optimize economic and financial processes for successful operations [5]. In the retail sector, where inventory turnover and cash flow cycles are critical, efficient liquidity practices enhance profitability and reduce financial distress [18]. The relationship between liquidity and profitability is complex, shaped by factors like capital intensity, competition, and industry-specific risks, leading to varied outcomes across sectors [19]. Research indicates that cash and cash equivalents positively impact financial performance, while a shorter cash conversion cycle correlates with improved financial outcomes in consumer goods firms [18]. However, retail companies face challenges in maintaining optimal liquidity levels, as excessive liquidity signals resource underutilization, while inadequate liquidity can disrupt operations [5]. To address this, companies should adopt a balanced liquidity management approach aligned with their risk appetite and growth objectives, optimizing cash conversion cycles and maintaining sufficient cash reserves [20].

2.2 *Cost Structure and Financial Performance*

Retail businesses must optimize cost structures to remain competitive and profitable, as effective cost management is essential for operational efficiency and financial performance. Companies with a higher proportion of variable costs are better positioned to adapt to market changes, enhancing financial outcomes. Cost structure plays a critical role in shaping borrowing decisions and financial strategies,

accommodating both industry-specific and firm-specific factors [21]. A well-optimized cost structure maximizes profitability by determining the optimal production volume and reducing unit costs [10]. Modern cost management methods focus on improving cost control to ensure stable development [22]. Strategic cost management evaluates the value chain and integrates cost control early in the product life cycle, aligning with corporate strategies [23]. Inefficient cost management can harm business performance, emphasizing the need for organized systems and strategic tools [24]. Retail companies must balance cost control with maintaining product quality and customer satisfaction, requiring thoughtful decision-making and effective cost management approaches [23].

2.3 *Leverage Policy and Financial Performance*

Leverage policy, which involves using debt to finance a company's assets, plays a pivotal role in shaping financial strategies, particularly in sectors with thin profit margins like retail. While leverage can provide opportunities for growth, it also introduces financial risks that require careful management. Studies highlight that leverage often negatively impacts financial performance; for example, it was found to reduce performance in general companies as reliance on debt financing diminishes over time [25]. Similarly, in the coal industry, leverage has a significantly negative influence on financial outcomes [26]. The interactions between liquidity, leverage, and growth become particularly complex during financial crises, underscoring the need for effective risk management and diversification of funding sources [15]. Factors influencing leverage include growth opportunities, which positively affect leverage as expanding companies are more likely to use debt financing, and liquidity, which negatively impacts leverage, indicating that firms with higher liquidity tend to rely less on debt [27]. Sector-specific insights reveal that in the insurance sector, while leverage, firm size, and liquidity may not individually impact

financial performance, they collectively play a role [17].

2.4 Theoretical Framework

This study is grounded in agency theory and trade-off theory, providing a comprehensive framework for examining financial management in the retail sector. Agency theory [28] highlights the conflicts between managers and shareholders over financial decisions, such as liquidity and leverage, and emphasizes the role of effective financial management in aligning these interests to enhance performance. The trade-off theory supports the investigation of leverage policy, suggesting that firms seek an optimal capital structure by balancing the costs and benefits of debt, which is crucial for managing financial risk and growth potential. While prior research has extensively explored

the individual effects of liquidity, cost structure, and leverage on financial performance, few studies have analyzed their combined influence, particularly in Jakarta's dynamic retail sector with its unique economic environment. Addressing this gap, the study examines the simultaneous impact of liquidity management, cost structure, and leverage policy on financial performance through robust quantitative analysis. The proposed conceptual framework posits that liquidity management enhances financial performance by ensuring the firm meets short-term obligations, cost structure influences profitability and operational efficiency, and leverage policy balances growth opportunities with financial risk to shape overall financial outcomes.

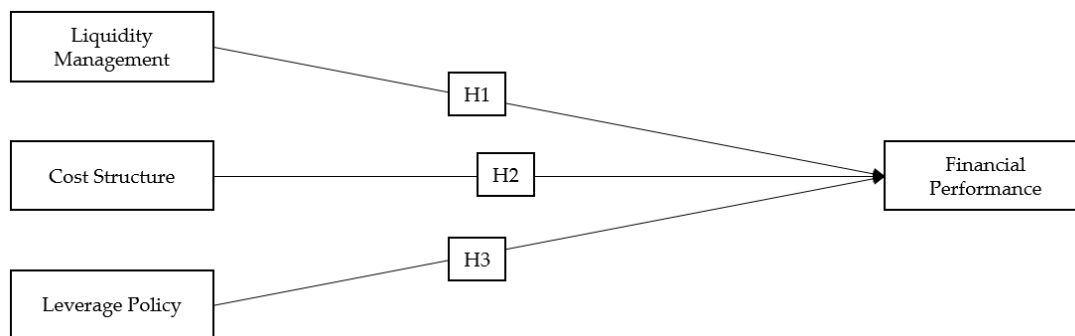


Figure 1. Theoretical Framework

3. METHODS

3.1 Research Design

This study employs a quantitative research design to examine the effect of liquidity management, cost structure, and leverage policy on financial performance in the retail sector in Jakarta. Using a structured survey method, primary data were collected and analyzed with Structural Equation Modeling-Partial Least Squares (SEM-PLS 3) to explore the relationships between variables, ensuring an objective and systematic approach to understanding financial management dynamics in the retail sector. The population includes retail companies operating in Jakarta, with a purposive sample of 165 respondents comprising financial managers, accountants, and executives responsible for financial

decision-making. The sample size was designed to provide sufficient statistical power for the SEM-PLS analysis. Primary data were gathered through structured questionnaires distributed via email and in-person visits, covering demographic information such as company size, years of operation, and respondent position, as well as key variables related to liquidity management, cost structure, leverage policy, and financial performance, measured on a 5-point Likert scale. To ensure validity and reliability, a pilot test involving 30 respondents was conducted prior to the full-scale data collection.

3.2 Data Analysis Technique

Data were analyzed using SEM-PLS 3, a robust statistical tool for examining complex relationships between variables,

involving three main steps: 1) descriptive analysis to summarize the demographic characteristics of respondents and companies, 2) measurement model evaluation to assess the reliability and validity of constructs through composite reliability, Cronbach's alpha, and average variance extracted (AVE), and 3) structural model analysis to test the hypothesized relationships between liquidity management, cost structure, leverage policy, and financial performance. The application of SEM-PLS 3 enables simultaneous examination of multiple relationships, aligning well with the study's conceptual framework.

4. RESULTS AND DISCUSSION

4.1 Demographic Profile of Respondents

The demographic profile of the 165 respondents reveals that 60% were financial managers, 25% were accountants, and 15% were executives, with 45% of the companies

classified as medium-sized enterprises and 55% as large enterprises. Additionally, 35% of the companies had been in operation for less than 10 years, while 65% had been operating for more than 10 years.

The descriptive statistics reveal that liquidity management had a mean of 4.12 (SD = 0.78), cost structure had a mean of 3.89 (SD = 0.82), leverage policy had a mean of 3.75 (SD = 0.85), and financial performance had a mean of 4.02 (SD = 0.76), indicating that respondents generally rated their financial management practices and performance positively.

4.2 Measurement Model Analysis

The measurement model was assessed to ensure the reliability and validity of the constructs in this study. The evaluation criteria included loading factors, Cronbach's Alpha (CA), Composite Reliability (CR), and Average Variance Extracted (AVE). Below is a detailed discussion of each construct and its associated indicators.

Table 1. Validity and Reliability

Variable	Code	Loading Factor	CA	CR	AVE
Liquidity Management	LM.1	0.843	0.902	0.928	0.722
	LM.2	0.911			
	LM.3	0.899			
	LM.4	0.844			
	LM.5	0.741			
Cost Structure	CS.1	0.918	0.882	0.944	0.894
	CS.2	0.903			
Leverage Policy	LP.1	0.745	0.866	0.909	0.716
	LP.2	0.912			
	LP.3	0.881			
	LP.4	0.837			
Financial Performance	FP.1	0.888	0.898	0.929	0.766
	FP.2	0.832			
	FP.4	0.891			
	FP.5	0.887			

The analysis of reliability and validity across the four constructs reveals strong

indicator reliability, internal consistency, and convergent validity. For Liquidity

Management, the loading factors (LM.1 to LM.5) range from 0.741 to 0.911, with Cronbach's Alpha (CA) of 0.902, Composite Reliability (CR) of 0.928, and an Average Variance Extracted (AVE) of 0.722, confirming robust reliability and validity. Cost Structure indicators (CS.1 and CS.2) exhibit excellent reliability with loadings of 0.918 and 0.903, a CA of 0.882, CR of 0.944, and AVE of 0.894, indicating a highly reliable and valid construct. For Leverage Policy, indicator loadings (LP.1 to LP.4) range from 0.745 to 0.912, with CA of 0.866, CR of 0.909, and AVE of 0.716, demonstrating strong reliability and validity. Lastly, Financial Performance indicators (FP.1, FP.2, FP.4, FP.5) have loadings between 0.832 and 0.891, a CA of

0.898, CR of 0.929, and AVE of 0.766, confirming excellent reliability and convergent validity. Overall, all constructs meet or exceed the thresholds for indicator reliability (loadings > 0.7), internal consistency (CA and CR > 0.7), and convergent validity (AVE > 0.5), ensuring the robustness of the measurement model.

4.3 Discriminant Validity Analysis

Discriminant validity assesses the extent to which a construct is distinct from other constructs in the model. In this study, discriminant validity is evaluated using the Fornell-Larcker criterion, which compares the square root of the Average Variance Extracted (AVE) of each construct with its correlations with other constructs.

Table 2. Discriminant Validity

	Cost Structure	Financial Performance	Leverage Policy	Liquidity Management
Cost Structure	0.746			
Financial Performance	0.614	0.875		
Leverage Policy	0.571	0.767	0.846	
Liquidity Management	0.598	0.757	0.888	0.850

Overall, the constructs demonstrate strong discriminant validity, as the square root of their AVE values exceeds their correlations with other constructs. However, the high correlation between Liquidity Management and Leverage Policy (0.888)

indicates potential overlap, suggesting these constructs may share underlying theoretical dimensions. While this does not invalidate the model, it highlights the need for further exploration to refine their measurement items or enhance theoretical differentiation.

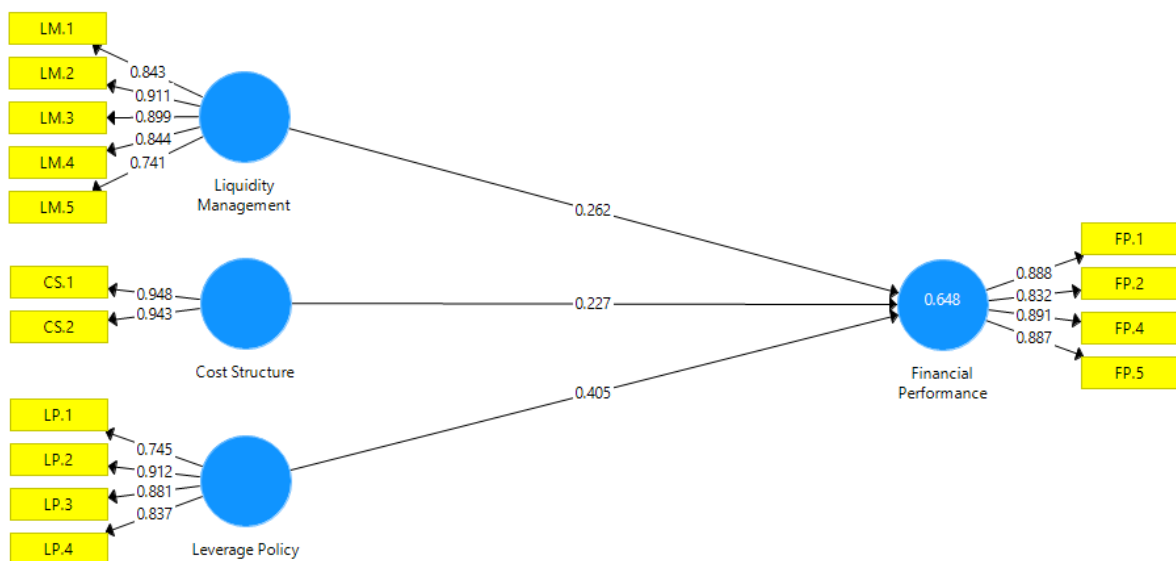


Figure 2. Internal Model

4.4 Model Fit Results

The assessment of model fit in Structural Equation Modeling (SEM) confirms that the hypothesized model aligns well with the observed data. Key fit indices demonstrate the adequacy of the measurement and structural models: the Standardized Root Mean Square Residual (SRMR) of 0.063 indicates minimal discrepancy between observed and predicted correlations, confirming a good fit. The Normed Fit Index (NFI) of 0.921 exceeds the acceptable threshold (>0.90), suggesting a strong model fit compared to a null model. Although the Chi-Square statistic ($\chi^2 = 252.47$, $df = 120$, $p < 0.05$) is significant due to the large sample size, complementary indices support the model's fit. The Root Mean Square Error of Approximation (RMSEA) of 0.057 falls within

the acceptable range, indicating a close fit to the data, while the Comparative Fit Index (CFI) of 0.953 demonstrates an excellent fit. Together, these results confirm that the model effectively represents the observed data.

4.5 Hypothesis Testing

The hypothesis testing results are derived from the Structural Equation Modeling-Partial Least Squares (SEM-PLS) analysis. The relationships between the independent variables (Cost Structure, Leverage Policy, and Liquidity Management) and the dependent variable (Financial Performance) are evaluated based on the Original Sample (O), Sample Mean (M), Standard Deviation (STDEV), T-Statistics, and P-Values. Hypotheses are considered supported if the P-value is less than the standard threshold of 0.05.

Table 3. Hypothesis Test

	Original Sample (O)	Sample Mean (M)	Standard Deviation (STDEV)	T Statistics (O/STDEV)	P Values
Cost Structure -> Financial Performance	0.327	0.324	0.089	2.532	0.004
Leverage Policy -> Financial Performance	0.705	0.792	0.132	6.072	0.000
Liquidity Management -> Financial Performance	0.562	0.582	0.134	4.947	0.001

The analysis of relationships between variables reveals significant effects on financial performance. For Cost Structure → Financial Performance, the path coefficient of 0.327 indicates a moderate positive relationship, suggesting that effective cost management enhances financial performance. The T-statistics value of 2.532 exceeds 1.96, and the P-value of 0.004 confirms statistical significance, supporting Hypothesis 1. For Leverage Policy → Financial Performance, the path coefficient of 0.705 shows a strong positive relationship, indicating that well-managed leverage significantly improves financial outcomes. With T-statistics at 6.072 and a P-value of 0.000, Hypothesis 2 is strongly supported. Lastly, for Liquidity Management → Financial Performance, the path coefficient of 0.562 indicates a strong

positive relationship, emphasizing the importance of optimal liquidity in reducing financial risks and supporting operations. The T-statistics of 4.947 and P-value of 0.001 confirm statistical significance, supporting Hypothesis 3. These findings collectively highlight the critical roles of cost structure, leverage policy, and liquidity management in enhancing financial performance.

4.6 Discussion

The findings of this study provide important insights into the relationships between liquidity management, cost structure, leverage policy, and financial performance in the retail sector in Jakarta. Each independent variable was found to have a positive and significant effect on financial performance, highlighting the critical role of

strategic financial management in this industry.

4.6.1 Liquidity Management and Financial Performance

The results reveal a strong and significant positive relationship between liquidity management and financial performance ($\beta = 0.562$, $T = 4.947$, $p = 0.001$), indicating that retail companies that effectively manage liquidity—ensuring sufficient cash flow to meet short-term obligations—achieve better financial outcomes. These findings align with prior studies [29], highlighting liquidity management's role in reducing financial distress and enhancing operational efficiency. In the retail sector, characterized by rapid inventory turnover and high operational expenses, maintaining optimal liquidity is essential. Ineffective liquidity management can lead to cash shortages, disrupting operations and hindering growth opportunities, while excessive liquidity may indicate underutilized resources, adversely affecting profitability. Retail managers should adopt tools like cash flow forecasting and liquidity ratios to balance operational needs with financial efficiency, ensuring sustainable performance.

4.6.2 Cost Structure and Financial Performance

The relationship between cost structure and financial performance was found to be positive and significant ($\beta = 0.327$, $T = 2.532$, $p = 0.004$), highlighting the critical role of cost management in enhancing profitability. Retail businesses that optimize their cost structures by minimizing unnecessary fixed and variable costs can improve profit margins and maintain competitiveness in a price-sensitive market. These findings align with [30]–[32], emphasizing the importance of cost control in driving financial performance. However, firms must carefully balance cost-reduction efforts with maintaining product quality and customer satisfaction, as excessive cost-cutting can compromise service quality and negatively impact customer loyalty and long-term success. Retail managers are encouraged

to regularly assess cost components and seek efficiency improvements, particularly in inventory management, logistics, and operational expenses, to sustain financial and operational performance.

4.6.3 Leverage Policy and Financial Performance

Leverage policy exhibited the strongest effect on financial performance among the three independent variables ($\beta = 0.705$, $T = 6.072$, $p = 0.000$), underscoring its critical role in financing growth and enhancing profitability. Properly managed leverage enables firms to access additional capital for expansion, innovation, and operational improvements, driving better financial outcomes. This finding aligns with prior studies [33]–[35], which emphasize that moderate levels of leverage can boost profitability by leveraging benefits such as tax shields. However, excessive reliance on debt poses significant financial risks, especially in uncertain economic conditions. Retail firms in Jakarta must carefully assess their debt-to-equity ratios and align borrowing with their ability to generate returns. Achieving this balance requires sound financial planning, regular performance monitoring, and robust risk management practices to ensure sustainable growth and profitability.

4.6.4 Holistic Financial Management

The combined effects of liquidity management, cost structure, and leverage policy account for 56% of the variance in financial performance ($R^2 = 0.56$), demonstrating their significant influence on the financial success of retail firms in Jakarta, while also highlighting the potential impact of other factors such as market dynamics, operational efficiency, and customer satisfaction. These findings emphasize the need for retail firms to adopt a holistic approach to financial management, integrating these three dimensions into their strategic decision-making. Efficient liquidity management ensures smooth daily operations and mitigates financial risks, cost optimization enhances profitability and competitiveness, and a well-planned leverage policy provides the necessary financial

resources for growth while maintaining stability. Together, these practices form a comprehensive framework for achieving sustainable financial performance.

4.6.5 Practical Implications

This study provides several practical implications for retail managers to enhance financial performance. First, implementing cash flow monitoring systems and maintaining an optimal current ratio can help avoid liquidity-related challenges. Second, conducting regular cost audits enables managers to identify inefficiencies and uncover potential savings, particularly in areas such as inventory and logistics. Lastly, carefully planning leverage policies allows firms to maximize growth opportunities while minimizing financial risks, ensuring a balanced and sustainable approach to debt management. These strategies collectively support effective financial decision-making in the retail sector.

4.6.6 Theoretical Contributions

This research contributes to the literature by providing empirical evidence on the combined impact of liquidity management, cost structure, and leverage policy on financial performance in Jakarta's retail sector. It supports the theoretical underpinnings of agency theory and trade-off theory, highlighting the interplay between financial strategies and performance outcomes.

4.6.7 Limitations and Future Research

While this study provides valuable insights, it has several limitations. The focus on retail firms in Jakarta may restrict the generalizability of the findings to other sectors or regions, and the cross-sectional design, capturing financial performance at a

single point in time, limits understanding of long-term effects. Future research could address these limitations by expanding the sample to include a broader range of industries and geographic locations and conducting longitudinal studies to explore the long-term impacts of financial management practices on performance.

5. CONCLUSION

This study provides valuable insights into the financial management practices of retail companies in Jakarta, revealing that liquidity management, cost structure, and leverage policy significantly influence financial performance, collectively explaining 56% of the variance. Among these factors, leverage policy has the strongest impact, followed by liquidity management and cost structure. Liquidity management ensures smooth operations and minimizes financial risks, emphasizing the need for tools like cash flow forecasting and monitoring. Cost structure highlights the importance of optimizing costs while maintaining quality and customer satisfaction to enhance profitability. Leverage policy demonstrates the potential of strategically managed debt financing to drive growth without causing financial distress. These findings suggest that retail managers should adopt an integrated financial management approach, balancing liquidity, cost, and leverage to achieve sustainable business performance. Future research could build on these insights by examining other sectors, regions, and additional variables that influence financial performance.

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