DIJEFA:
Dinasti International Journal of Economics, Finance & Accounting
E-ISSN: 2721-303X
P-ISSN: 2721-3021
https://dinastipub.org/DIJEFA dinasti.info@gmail.com +62 811 7404 455
DOI: https://doi.org/10.38035/dijefa.v6i3

Free Cash Flow, Leverage, and Firm Value: The Moderating Role of Managerial Ownership

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Abstract: The firm value represented by its share price often fluctuates. To select profitable investments, investors must be able to estimate firm value. The purpose of this study is to gather empirical evidence regarding the influence of free cash flow and leverage on firm value, and how managerial ownership moderates this influence. The study population includes all companies listed on the Indonesia Stock Exchange between 2021 and 2023, with a sample of 760 companies and 2,016 observations. Purposive sampling was used to choose the sample. This study uses moderated regression analysis with STATA application. The findings indicate that free cash flow has a positive effect on firm value, while leverage has no effect on firm value. On the other hand, managerial ownership does not play a role in moderating the effect of free cash flow and leverage on firm value.

Keyword: Firm Value, Free Cash Flow, Leverage, Managerial Ownership

INTRODUCTION

Increasing firm value is one of the main objectives of a company. Stock prices are often used as a benchmark of company value for companies that offer shares on the capital market. The IDX Composite Index (ICI) is an indicator that shows the increase or decrease in the overall stock prices of companies listed on the Indonesia Stock Exchange (IDX). According to data from the IDX, the ICI increased by 4.09 percent from 2021 to 2022. Then, from 2022 to 2023, it rose again by 6.16 percent. Despite the increase in the ICI, sectoral index in each sector experienced fluctuations. These fluctuations were influenced by various factors, so investors must have the ability to predict firm values. Investors require various information to analyze the market and make investment decisions (Rasid & Hafizi, 2022).

According to signaling theory by Spence (1973), information in financial statements can be used as signals by users to identify the condition of a company. Financial information that shareholders pay attention in order to predict the value of a company is free cash flow. Free cash flow is defined as the remaining cash available after operating cash inflows have been allocated to pay all working capital and investment costs (Ross et al., 2022). The presence of free cash flow indicates that a company has successfully achieved good performance with the ability to generate cash from its operating activities, resulting in excess cash (Utami & Astika, 2024). The findings of a studies by Aisyah et al. (2023), Rahmi & Wijaya (2022), and

Pradnyani et al. (2021) show that free cash flow contributes positively to raise the firm's value. Meanwhile, research by Dewi & Erawati (2024), Erawati & Jedaru (2023), and Bahrun et al. (2020) found a negative contribution of free cash flow to firm value. Other findings were reported by Nurwanto (2022), Sugiharto & Hendratno (2022), and Wibowo et al. (2021) which indicated that free cash flow has no significant impact on firm value.

In addition to using cash flow generated internally, a company's operating funds can come from external sources. These funds can come from company debt. The level of debt can be assessed through the leverage. Leverage is defined as the ratio that describes the extent to which a company's funds come from debt (Sari & Wirawati, 2024). Financing using debt is not always beneficial for a company. Research by Hermuningsih et al. (2022), Kristi & Yanto (2020), and Setiyowati et al. (2020) indicate that leverage negatively contributes to firm value. However, findings by Dwianto et al. (2023), Hapsoro & Bahantwelu (2020), and Radja & Artini (2020) suggest that leverage has a positive impact on firm value. Different findings were reported in studies by Mayzona & Rusmanto (2025), Habakkuk et al. (2023), and Firmansyah et al. (2020), which concluded that the company value is not significantly impacted by leverage.

Previous studies examining the influence of free cash flow and leverage on firm value have shown inconsistent results. According to Govindarajan (1986), a contingency framework can resolve the conflicting results of previous studies by using moderating variables. The moderating variable selected in this study is managerial ownership. This variable describes the share ownership held by the company's managers. Managerial ownership helps minimize agency conflicts by bringing managers' and shareholders' interests into alignment, according to Jensen & Meckling's (1976) agency theory.

This study purposed to analyze whether free cash flow and leverage can influence firm value, as well as how the level of managerial ownership within a company can moderate this influence. This study differs from earlier research in that it identifies the influence of free cash flow on firm value by considering the moderation of managerial ownership, analyzing all companies listed on the Indonesia Stock Exchange (IDX) between 2021 and 2023 as the population, and incorporating control variables to prevent the effect of outside factors that not considered in this research model.

A company with high free cash flow may indicate the availability of cash that can be allocated for various purposes, such as paying debts, paying dividends, and expanding business expansion, which will have a positive contribution on the company (Rahmi & Wijaya, 2022). A company can be considered healthier if it can generate greater free cash flow because it has sufficient cash availability (Wahyuni & Badera, 2020). According to signaling theory, high free cash flow can be an indication of successful business performance, thereby generating positive signals that will encourage investors to purchase shares, so contributing for increasing the firm value (Yulianti et al., 2021). Research findings by Utami & Astika (2024), Aisyah et al. (2023), Rahmi & Wijaya (2022), Pradnyani et al. (2021), and Yulianti et al. (2021) show that the company value is positively impacted by free cash flow.

H1: Free cash flow has a positive effect on firm value.

According to signaling theory, the use of debt as a source of corporate financing can send a negative signal that causes investors to reconsider investing (Tjahjani et al., 2024). The use of debt with poor management can lead to an increase in principal and interest expenses, which can cause a decline in profitability or even losses (Setiyowati et al., 2020). High debt financing can also increase the risk of liquidation, thereby sending a negative signal that reduces investor confidence in investing their capital (Kristi & Yanto, 2020). This statement is supported by the research results of Prieto et al. (2024), Yusphita & Ekawati (2023), Simanjuntak & Hasibuan (2023), Hermuningsih et al. (2022), Hidayat (2022), and Kristi & Yanto (2020) also indicate that leverage levels have a negative impact on firm value.

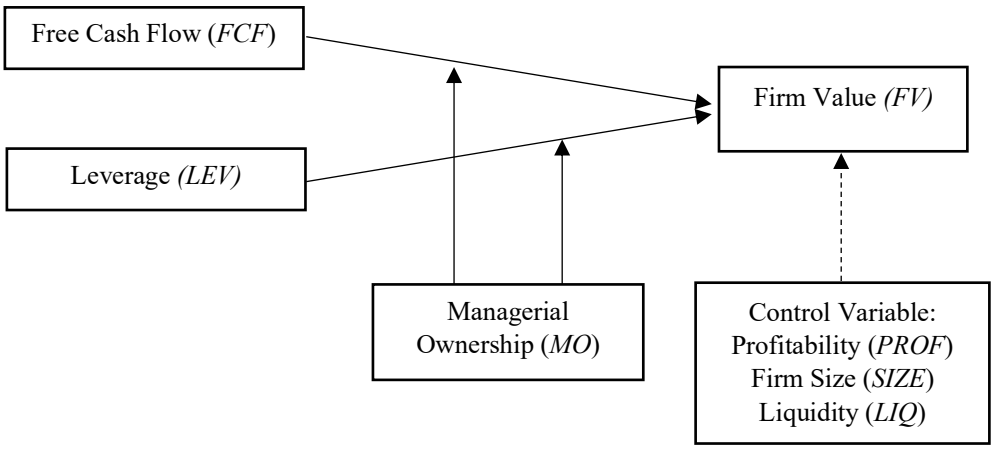
H2: Leverage has a negative effect on firm value.

According to agency theory, managerial ownership can prevent managers from prioritizing their own interests by controlling free cash flow to increase incentives for themselves (Yulianti et al., 2021). Managers will feel the direct consequences of the decisions they make. If those decisions cause a decline in the value of the company, managers will suffer the same losses as other shareholders (Dewi & Badera, 2021). In relation to signaling theory, the presence of managerial ownership can be interpreted as a positive signal for investors. High managerial ownership fosters confidence that managers will strive to improve shareholder welfare by increasing firm value. Previous studies by Susbiyani & Animah (2024), Suratman & Ismedt (2023), Ifada et al. (2021), Benson et al. (2020), and Soewarno & Ramadhan (2020) indicate that an increase in managerial ownership will have implications for an increase in firm value. These results show the potential of managerial ownership to strengthen the influence of free cash flow in contributing to rise the firm value.

H3: Managerial ownership strengthens the effect of free cash flow on firm value.

In line with agency theory, managers with significant shareholdings in the companies they work for will tend to allocate leverage wisely so as not to increase the risk of bankruptcy (Ermawati & Triyono, 2024). In line with signaling theory, managerial ownership can serve as a positive signal, as it can instill investor confidence that managers will use funds obtained through debt more effectively and efficiently. Findings from research by Suratman & Ismedt (2023), Ifada et al. (2021), Benson et al. (2020), and Soewarno & Ramadhan (2020) show that managerial ownership has the potential to rise firm value. These studies are reinforced by findings from studies by Lubis et al. (2025) and Doorasamy (2021), which found that managerial ownership plays moderating role in the relationship between capital structure (leverage) and firm value.

H4: Managerial ownership weakens the effect of leverage on firm value.



Source: Research Data, 2025

Figure 1. Conceptual Framework

METHOD

A quantitative approach in the form of association with non-participant observation data collection methods was used in this research. The data used are secondary data collected from audited financial statements, company annual reports, and the Thomson Reuters Refinitiv Eikon database. The population includes all firms registered on the Indonesia Stock Exchange between 2021 and 2023. Purposive and nonprobability sampling methods were used to choose the sample.

According to Hermuningsih et al. (2022), firm value is a figure that represents how investors view a company in relation to its share price. In this study, Tobin's Q is used as an

indicator of company value, calculated using the following formula (Hermuningsih et al., 2022).

$$FV_{i,t} = \frac{((\text{Stock Price} \times \text{Number of Shares Outstanding}) + \text{Total Debt})}{\text{Total Assets}} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots(1)$$

The definition of free cash flow is cash produced by operational activity of company that remains after the company has fulfilled all of its obligations and operating expenses. In this study, free cash flow is assessed using the following calculation (Wibowo et al., 2021).

$$FCF_{i,t} = \frac{\text{Operating Cash Flow} - \text{Net Capital Expenditure} - \text{Net Working Capital}}{\text{Total Assets}} \quad \ldots(2)$$

Leverage can be measured by the debt to equity ratio (DER), which can represent the high or low value of a company's debt. An increasing DER value indicates that the proportion of debt in the company is higher than its equity. The DER is calculated as follows (Loriyani & Mimba, 2023).

$$LEV_{i,t} = \frac{\text{Total Debt}}{\text{Total Equity}} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(3)$$

Managerial ownership is defined to the holding of shares by individuals who are also in management positions inside the organization. The value of managerial ownership is calculated as follows (Ifada et al., 2021).

$$MO_{i,t} = \frac{\text{Number of Shares Owned by Management}}{\text{Number of Shares Outstanding}} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(4)$$

Profitability, using the return on equity (ROE) ratio as a proxy, reflects the level of efficiency in the capital management of a company. The following formula is used to determine profitability (Sihombing & Zakchona, 2024).

$$PROF_{i,t} = \frac{\text{Net Income}}{\text{Shareholders Equity}} \times 100\% \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(5)$$

Firm size is the scale of classification of the size of a company. The natural logarithm of total assets can be used to measure the firm size. The following formula is used to determine a company's size (Wibowo et al., 2021).

$$SIZE_{i,t} = \text{Ln (Total Assets)} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(6)$$

Liquidity refers to the ability of a company to settle its short-term debts. Liquidity is measured by the current ratio, which is computed using the method below (Sari & Wirawati, 2024).

$$LIQ_{i,t} = \frac{\text{Current Assets}}{\text{Current Liabilities}} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(7)$$

The data analysis stages involved descriptive statistical analysis followed by classical assumption testing before performing regression analysis. The regression test in this study applied moderated regression analysis (MRA) using STATA 17 software. The purpose of using MRA was to determine whether the managerial ownership variable had a moderating role in the influence of free cash flow and leverage variables on firm value. The results of the model feasibility test (F test), coefficient of determination test (adjusted R-squared), and partial test (t test) were acquired following the completion of moderated regression analysis. The MRA test equation model in this study is as follows:

$$FV_{i,t} = \beta_0 + \beta_1 FCF_{i,t} + \beta_2 LEV_{i,t} + \beta_3 MO_{i,t} + \beta_4 FCF_{i,t} MO_{i,t} + \beta_5 LEV_{i,t} MO_{i,t} + \beta_6 PROF_{i,t} + \beta_7 SIZE_{i,t} + \beta_8 LIQ_{i,t} + \varepsilon_{i,t} \quad \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(8)$$

Description:

$FV_{i,t}$: Firm value

β_0 : Constant

$\beta_1, \ldots, \beta_8$: Regression coefficient

$FCF_{i,t}$: Free cash flow
$LEV_{i,t}$: Leverage
$MO_{i,t}$: Managerial ownership
$FCF_{i,t}MO_{i,t}$: Interaction between free cash flow and managerial ownership
$LEV_{i,t}MO_{i,t}$: Interaction between leverage and managerial ownership
$PROF_{i,t}$: Profitability
$SIZE_{i,t}$: Firm size
$LIQ_{i,t}$: Liquidity
$\varepsilon_{i,t}$: Residual

RESULTS AND DISCUSSION

Samples were selected using criteria based on purposive sampling methods as shown in Table 1.

Table 1. Determination of Research Samples

Criteria	Year			Total
	2021	2022	2023	
Companies listed on the IDX during the research period.	766	823	902	2,491
Financial sector companies listed on the IDX during the research period.	(103)	(104)	(104)	(311)
Companies that were suspended during the research period.	(34)	(40)	(47)	(121)
Eliminate outlier data.	(15)	(13)	(15)	(43)
Samples used.	614	666	736	2,016
Number of observations during 2021-2023				**2,016**

Source: Research Data, 2025

In the selected data, outlier data was found. Outlier data is data with values that are significantly different from other observation data in the form of extreme values (Ghozali, 2021). Data classified as outliers based on standardized scores greater than three will be eliminated from the sample to obtain more representative results.

Table 2. Results of Descriptive Statistical Analysis

Variable	Number of Obs.	Mean	Standard Deviation	Minimum Value	Maximum Value
FV	2,016	2.109	5.459	0.085	124.120
FCF	2,016	-0.144	0.427	-1.571	4.726
LEV	2,016	0.953	2.769	-30.153	29.317
MO	2,016	0.082	0.180	0	0.925
PROF	2,016	0.062	0.115	-0.138	0.259
SIZE	2,016	28.196	1.852	24.704	32.206
LIQ	2,016	2.894	3.494	0.142	18.765

Source: Research Data, 2025

Based on Table 2, FV has a minimum value of 0.085 and a maximum value of 124.120. The mean value is 2.109, which is close to its minimum value, indicating that the firm value is classified as low. The standard deviation of this variable is 5.459, which exceeds the average value, indicating a heterogeneous distribution of the variable. FCF has a minimum value of -1.571 and a maximum value of 4.726. Its mean value is close to its minimum value, which is -0.144, indicating a low level of FCF. The standard deviation of this variable is 0.427, which is greater than its average, indicating that this variable has a heterogeneous distribution. LEV has a minimum value of -30.153 and a maximum value of 29.317. Its mean value is close to its

maximum value, which is 0.953, indicating a high level of leverage. The standard deviation is 2.769, which exceeds the mean value, indicating a heterogeneous distribution of the variable. MO has a minimum value of 0 and a maximum value of 0.925. Its mean value is 0.082, which is close to its minimum value, indicating a low level of managerial ownership. The standard deviation of this variable is 0.180, which exceeds its mean value, indicating that the variable has a heterogeneous distribution.

PROF has a minimum value of -0.138 and a maximum value of 0.259. The mean value is 0.062, which is closer to the maximum value, indicating a high level of profitability. The standard deviation of profitability is 0.115, which exceeds the mean value, indicating a heterogeneous distribution of the variable. SIZE has a minimum value of 24.704 and a maximum value of 32.206. Its mean value is 28.196, which is closer to its minimum value, indicating that the company size is classified as low. The standard deviation of this variable is 1.852, which is below the mean value, indicating that this variable has a homogeneous level of dispersion. LIQ has a minimum value of 0.142 and a maximum value of 18.765. The mean value is 2.894, which is close to the minimum value, indicating that the liquidity level is low. The standard deviation of this variable is 3.494, which is greater than the mean value, indicating that this variable has a heterogeneous distribution.

Table 3. Summary of Classical Assumption Test Results

	Normality	Multicollinearity	Heteroscedasticity	Autocorrelation
	Prob>z	VIF	Prob > chi2	Prob > F
FCF	0.00001	1.48	0.1393	0.9415
LEV		1.13		
MO		2.11		
FCFMO		1.87		
LEVMO		1.39		
PROF		1.14		
SIZE		1.25		
LIQ		1.47		

Source: Research Data, 2025

The Shapiro–Francia normality test yielded a Prob>z value of 0.00001, which is < 0.05, indicating the non-normal distribution of the variables residual values. According to the Central Limit Theorem (CLT), the normality assumption can be ignored if the study's sample size is large enough. The CLT states that the distribution of a sample will converge closer to a normal distribution as the sample size grows (Pek et al., 2018). According to the CLT, if the sample size is 30 or more, then the distribution of the sample can be said to approach a standard normal distribution (Kwak & Kim, 2017).

The multicollinearity test conducted based on the analysis of the Variance Inflation Factor (VIF) values resulted in individual VIF values for all variables less than 5. Based on this, it can be stated that multicollinearity was not found in the model. The heteroscedasticity test conducted using the White test showed a Prob > chi2 value of 0.1393. This value indicates a significance level higher than 0.05, indicating that that heteroscedasticity was not found in the model. The autocorrelation test using the Wooldridge test showed a Prob > F value of 0.9415, which is also greater than 0.05, indicating that there are no autocorrelation in this research model.

Table 4. Moderated Regression Analysis Results

FV	Coefficient	Std. err.	t	Sig.
FCF	0.999	0.342	2.92	0.004
LEV	0.047	0.046	1.01	0.314
MO	-0.222	0.969	-0.23	0.819
FCFMO	1.890	1.852	1.02	0.308

LEVMO	0.004	0.515	0.01	0.994
PROF	3.160	1.116	2.83	0.005
SIZE	-0.431	0.073	-5.94	0.000
LIQ	0.098	0.042	2.34	0.019
Cons	13.949	2.067	6.75	0.000
F-Statistics	=	6.48		
Sig. F	=	0.0000		
R-squared	=	0.0252		
Adj R-squared	=	0.0213		

Source: Research Data, 2025

Based on Table 4, the equation from the MRA test results can be formulated as follows.

$$FV_{i,t} = 13.949 + 0.999\ FCF_{i,t} + 0.047\ LEV_{i,t} - 0.222\ MO_{i,t} + 1.890\ FCF_{i,t}MO_{i,t} + 0.004\ LEV_{i,t}MO_{i,t} + 3.160\ PROF_{i,t} - 0.431\ SIZE_{i,t} + 0.098\ LIQ_{i,t} + \varepsilon_{i,t}$$

Based on Table 4, the constant value of 13.949 indicates that if the values of free cash flow, leverage, managerial ownership, the interaction between free cash flow and leverage with managerial ownership, profitability, company size, and liquidity are zero, then the firm's value will be 13.949. A significance level of 0.0000 is displayed by the F-test, indicating that the result is less than the 0.05 threshold. Based on this results, it can be interpreted that the regression model is suitable for use. The determination coefficient can be analyzed based on the adjusted R-squared value. According to Table 4, the adjusted R-squared value is 0.0213, or 2.13 percent. This result represents that the free cash flow, leverage, managerial ownership, interaction of the two independent variables with the moderating variable, profitability, company size, and liquidity, can explain 2.13 percent of the firm value variable. Meanwhile, the remaining percentage is explained by additional outside variables not covered by the model.

The first hypothesis states that free cash flow has a positive effect on firm value. The findings from the regression analysis show that the t-test produced a significance value for this variable of 0.004, which is less than the 0.05 significance level. The regression coefficient value obtained is positive 0.999. Based on the analysis of these figures, the first hypothesis is accepted, indicating that free cash flow has a favorable impact on firm value. According to the study's findings, a rise in free cash flow is followed by a rise in firm value. On the other hand, if a company's free cash flow declines, its firm value will also fall.

High free cash flow in a company can increase shareholder confidence to invest. The company is considered to be performing well, so it has excess cash that can be allocated to pay debts, pay dividends, increase company growth, and survive in difficult conditions. The value of the firm will increase as the number of investors investing capital increases. These results align with the findings of studies by Utami & Astika (2024), Aisyah et al. (2023), Rahmi & Wijaya (2022), Pradnyani et al. (2021), and Yulianti et al. (2021). These findings support the signaling theory, which states that shareholders, as recipients of information provided by company managers as information providers, can obtain signals from information in financial statements. A high level of free cash flow in a company will send a positive signal that can be received by investors, which can then encourage investment that impacts an increase in firm value.

The second hypothesis states that leverage has a negative effect on firm value. Based on the t-test, a regression coefficient of 0.047 was obtained for the leverage variable, which is positive, and a significance level of 0.314, which exceeds the significance of 0.05. Analysis of these results indicates rejection of the second hypothesis and shows that the firm value is not significantly impacted by the amount of leverage. This result shows that, regardless of how high or low the leverage is, it has no impact on the company's value.

External funding has become commonplace, especially for companies in a phase of rapid growth, because internal sources of funding are often insufficient to meet significant

growth needs. When making investment selections, investors don't give much thought to how much debt a company uses to finance its operations. Investors typically focus more on how management allocates funds, whether it has been done optimally or not. This result indicates that the proportion of debt use has no significant impact on the value of the firm. This result aligns with the research findings by Mayzona & Rusmanto (2025), Djuharni et al. (2024), R.Win & Hasibuan (2024), Habakkuk et al. (2023), and Firmansyah et al. (2020), who stated that the leverage ratio is unable to significantly influence increases or decreases in firm value.

The third hypothesis states that managerial ownership strengthens the effect of free cash flow on firm value. Based on the t-test results, it is shown that the interaction variable between free cash flow and managerial ownership obtained a positive regression coefficient of 1.890. The level of significance recorded was 0.308, which above the 0.05 threshold for significance. Based on the analysis of this result, it can be interpreted that this finding contradicts the third hypothesis, so the third hypothesis is rejected. Therefore, the study's findings indicate that managerial ownership cannot strengthen the influence of free cash flow on the value of the firm.

The existence of managerial ownership has not been able to increase manager's motivation in allocating free cash flow to increase the value of the firm. An increase in managerial ownership has not been able to reduce agency conflict because managerial ownership has not been able to align the interests of management with those of shareholders (Bakhtiar et al., 2020). This may be due to the fact that managerial ownership in companies listed on the Indonesia Stock Exchange (IDX) in 2021-2023 is relatively low. Low managerial ownership means that managers do not feel a sense of ownership towards the company because they only enjoy a small portion of the profits as shareholders (Dewi & Widhiyani, 2023). These findings are supported by the research of Suwarti et al. (2023), Malelak et al. (2020), Bakhtiar et al. (2020), and Ekaputra et al. (2020), who found that managerial ownership does not significantly influence the rise and fall of the value of the firm.

The fourth hypothesis states that managerial ownership weakens the effect of leverage on firm value. According to the t-test results, the regression coefficient for the interaction variable between leverage and managerial ownership is positive at 0.004, with a significance level of 0.994. This value exceeds the significance level of 0.05. The analysis of these figures indicates that this finding does not support the fourth hypothesis, so the fourth hypothesis is rejected. The findings indicate that the influence of leverage on firm value is not moderated or weakened by managerial ownership.

The existence of shares owned by manager is not sufficient to improve the optimal use of company resources by management, especially when managing external funding sources. This condition may be caused by the relatively low level of managerial ownership in the companies. Low managerial ownership may cause managers to lack a sense of firm ownership because of the small ownership percentage, so that management are not significantly impacted if the firm's value declines as a result of using debt. This is in line with research by Adinegara & Herliansyah (2023), which states that low managerial share ownership causes management to not feel the losses due to a decline in the value of the firm because they do not have significant ownership in the company. This causes managers to pay less attention to the interests of the company, including the efficient use of external funds. This study's results are consistent with the findings of Astuti & Murwani (2022), who found that managerial ownership does not play a role in moderating the influence of the debt-to-equity ratio (DER) on firm value. Additionally, these result support the findings of Suwarti et al. (2023), Malelak et al. (2020), Bakhtiar et al. (2020), and Ekaputra et al. (2020) which state that the fluctuations in firm value are not significantly impacted by managerial ownership.

CONCLUSION

There are several conclusions from the study about the effects of free cash flow and leverage on firm value, with managerial ownership as a moderating variable. First, free cash flow has a positive effect on firm value. Second, leverage has no effect on firm value. Third, managerial ownership cannot strengthen the effect of free cash flow on firm value. Fourth, managerial ownership also cannot weaken the effect of leverage on firm value.

The limitations of this study lie in the capacity of the independent factors, moderation, and control to explain the dependent variable, which as indicated by the adjusted R-squared value, is just 2.13 percent. It is suggested that future studies incorporate more factors that could affect firm value. Furthermore, this study was unable to explain the inconsistencies found in previous research, as the results show that managerial ownership has no moderating role on the effect of free cash flow and leverage on firm value. Researchers in the future who want to carry out comparable studies may explore other variables that may act as moderating variables, such as using the good corporate governance (GCG) index or other GCG mechanisms.

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