DETERMINANTS OF CAPITAL STRUCTURE OF PAKISTANI LISTED COMPANIES: THEORY VS. PRACTICE

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Abstract

This paper establishes a prelude research to discover the determinants of capital structure of Pakistani listed companies using data at the firm level. The findings show that most of the companies tend to maintain financing hierarchy in a desire to enhance, the firm value. Avoiding control dilution is a key purpose of following pecking order approach, rather than target capital strategy. The firm size, cost of capital, profitability and operating performance, asset tangibility, and tax implications were tested with capital structure on a sample of fifty firms. Cost of debt and equity, and profitability were directly related to leverage while asset tangibility, operating performance, taxes and the firm size were inversely related. Results inconsistent with capital structure theories included asset tangibility and the firm size to be significantly and negatively related to the firm’s gearing though theory suggested them to be positively related. All variables included in this research showed significant impact on capital structure.

Keywords: Capital Structure, Pecking Order, Static Trade-off, Financing Hierarchy.

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