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IMPACT OF CAPITAL STRUCTURE ON PERFORMANCE OF MALAYSIAN TRADING AND SERVICE FIRMS

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Abstract

The objective of the study is to scrutinize an association between capital structure with trading and services firm's performance listed in Malaysia stock exchange (Bursa Malaysia). The data collected and retrieved from the trading and services company cover from period of 2008 to 2017 which are gathered from Bursa Malaysia, Bloomberg and Thomson Data Stream. Throughout, this study uses multivariate regressions to analyze the entire dependent variables for trading and services firm's performance with its independent variables. In overall, the results show that there are a statistically significant relationship between the capital structure towards trading and services firm's performance. Thus, from the findings, it can provide a reference to trading and services firms and stakeholders to predict the impact of permissible return (yields) to them since this study revealed a new knowledge on the relationship of capital structure towards trading and services sectors which is still under research in Malaysia.

1. Introduction

In the capital structure, its normally consist of debt and equity that funded the business management. Debt leverage is an efficient way to reduce free cash flows and enhance firm performance. Akeem et al. (2014) revealed a positive influence on firm performance by debt leverage; however, Javed et al. (2014) have an inverse argument that leverage is negatively related to growth and profitability performance.

Basit and Hassan (2017) studies about the impact of capital structure on firm's performance. The studied found that capital structure negative relation with ROA but positive relation between capital structure and Return on Equity.

The result demonstrates that firm's performance, which are measured by return on asset and return on equity have negative relationship with independent variables, which is total debt, short-term debt and long-term debt (Salim & Yadev, 2012).

2. Problem Statement

Extant studies have investigated the relationship between capital and profitability (Chowdhury & Chowdhury, 2010; Ebrati et al., 2013; Ebaid, 2009; Pouraghajan et al., 2012) to name few; however, all of the studies thus not particularly focus on the trading and services firms performance. Given that, trading and services industry in Malaysia is growing with significant contribution in uplifting the economic, thus, finding the importance of its capital management is also crucial. These objectives motivated the study to explore the relationship between capital structure with trading and services firm performance in Malaysia since its still under-research focused on long-term and short-term debt.

3. Research Questions

1. To analyze the current status of capital structure among trading and services firms in Malaysia,

2. To examine the relationship between the short term and long-term capital structure with trading and services firms' performance.

4. Purpose of the Study

1. To investigate its effects on capital structure because only few studies have examined this relationship in Malaysia context.

2. To discover the level, to which debt that are differentiating into the long term, short term and total debt that will affect firm performance.

3. To help to value add their investment decisions on the firms under scrutiny.

4. To help Bank Negara Malaysia and Securities Commission to monitor the development of capital structure in Malaysia.

5. Research Methods

The sample size in this study consists of 30 public listed trading and service companies in Bursa Malaysia covers for a period from 2008 to 2017 on an annual basis. The data collected from Thomson Reuters, companies' annual report, and central bank and Bloomberg software.

Table 01. Dependent and independent variables

Variables	Proxies
Dependent Trading and Service Firm's Performance	Return On Asset (ROA) Return on Equity (ROE)
Independent Capital Structure	Long term debt to total asset (LTTA) Short term debt to Total Assets (STTA) Total debt to Total Assets (TDTA) Total debt to total equity(TDTE)

This research study is tested the relationship between firms' performance and capital structure, thus, multiple regression model applied. The multiple regression equations can be represented as follows:

$$ROA_{it} = \alpha + \beta 1 LTTA1_{it} + \beta 2 STTA2_{it} + \beta 3 TDTA3_{it} + \beta 4 TDTE4_{it} + \varepsilon_{it} \quad (1)$$

$$ROE_{it} = \alpha + \beta 1\ LTTA\ 1_{it} + \beta 2\ STTA\ 2_{it} + \beta 3\ TDTA\ 3_{it} + \beta 4\ TDTE\ 4_{it} + \varepsilon_{it} \quad (2)$$

Where,

ROA = Return On Asset

ROE = Return on Equity

LTTA = Long term debt to total asset

STTA =Short term debt to Total Assets

TDTA = Total debt to Total Assets

TDTE = Total debt to total equity

6. Findings

6.1. Pearson Correlations Results

As reported in Table 02, Pairwise correlations among independent variables might be high (in absolute value). If the correlation > 0.8 then severe multicollinearity may be present. The significant values were not seriously affected by the presence of multicollinearity since all values reports below than 0.8 except for long-term debt to total asset stands at 0.833.

Table 02. Pearson Correlations

		Total debt to total asset	Total debt to total equity	Short term debt to total asset	Long term debt to total asset	ROE	ROA
Total debt to total asset	Pearson correlation	1	.387**	.135*	.833**	-.124*	-.089
	Sig. (2-tailed)		.000	.019	.000	.032	.126
	N	300	300	300	300	300	300
Total debt to total equity	Pearson correlation	.387**	1	.012	.569**	.703**	-.036
	Sig. (2-tailed)	.000		.841	.000	.000	.530
	N	300	300	300	300	300	300
Short term debt to total asset	Pearson correlation	.135*	.012	1	-.221**	.033	-.009
	Sig. (2-tailed)	.019	.841		.000	.563	.877
	N	300	300	300	300	300	300
Long term debt to total asset	Pearson correlation	.833**	.569**	-2.21**	1	.103	-.007
	Sig. (2-tailed)	.000	.000	.000		.074	.904
	N	300	300	300	300	300	300
ROE	Pearson correlation	-.124*	.703**	.033	.103	1	.202**
	Sig. (2-tailed)	.032	.000	.563	.074		.000
	N	300	300	300	300	300	300
	Pearson correlation	-.089	-.036	-.009	-0.07	.202**	1
	Sig. (2-tailed)	.126	.530	.877	.904	.000	
	N	300	300	300	300	300	300

6.2. Multivariate regression was used to analyse between each independent variable (TDTA, TDTA, STTA and LTTA with dependant variable (ROA and ROE). It was tested with significant value $\alpha = 0.05$.

6.2.1. The Relationship between TDTA, TDTE, STTA and LTTA with ROE.

Table 03. Regression

	Coefficients	t	p-value
(Constant)	0.372	5.639	0.000
TDTA	-3.812	-7.441	0.000
TDTE	0.415	19.741	0.000
STTA	2.232	2.981	0.003
LTTA	0.980	1.479	0.140

Dependent Variable: ROE

The estimated regression equation for Return on Equity (ROE)

ROE = 0.372+ 2.232STTA+ 0.980LTTA− 3.812TDTA+0.415TDTE+ ε

$R^2 = 0.689$

F-value= 163.068 (0.000)

In term of ROE as refer to the Table 04, the results indicate a significant positive relationship between STTA (+2.232) and TDTE (0.415) at 1% significant level with ROE. However, negative relationship was depicted for TDTA (-3.812). Yet, based on r square =0.689, only 68.9% percent of the amount of variation in ROE can be an attributed to STTA, TDTE, LTTA and TDTA. Since p value =0.000 < 0.05, it was found there are have significant in between TDTA, TDTE, STTA With ROE except LTTA.

6.2.2 The Relationship Between TDTA, TDTE, STTA and LTTA with ROA.

Table 04. Regression

	Coefficients	**t**	**p-value**
(Constant)	0.041	6.724	0.000
TDTA	-0.171	-3.619	0.000
TDTE	-0.004	-1.951	0.042
STTA	0.158	2.280	0.023
LTTA	0.205	3.342	0.001

a. Dependent Variable: ROA

The estimated regression equation for Return on Equity (ROE)

ROA = 0.041+ 0.158STTA+ 0.205LTTA− 0.1712TDTA- 0.004TDTE+ ε

R^2 = 0.044

F-Value = 3.398 (0.010)

In term of ROA as refer to the Table 06, the results indicate a significant positive relationship between STTA (+0.158) and LTTA (+0.205) at 1% significant level with ROE. However, negative relationship was depicted for TDTA (-0.171) and TDTE (-0.004). Yet, based on r square =0.044, only 4.4% percent of the amount of variation in Return On Asset can be a attributed to STTA, TDTE, LTTA and TDTA. Since p value =0.010 < 0.05, it was found there are have significant in between TDTA, TDTE, STTA and LTTA with ROA. However, the adjusted R-square (0.044) is relatively low thus indicating only 4.4% of the changes respectively in the ROA was explained by the changes in the capital structure variables in the model. The remaining 95.6% of the changes respectively are explained by other factors not in the model.

7. Conclusion

This study integrates the findings on the impact of capital structure on trading and service firm performance. The regression results support objective 1 and 2 as showed in Table 03 and table 04 that the F statistics is substantiated at the 1% significant level for ROE (163.068) and ROA (3.398). The study concluded that capital structure has a significant relationship with firm performance (Ahmad et al., 2012). It was explaining that firm's capital structure owned by the trading and services firms could be significantly contribute to the profitability performance in Malaysia (Salim & Yadev, 2012). Thus, from the findings, it can provide a reference to trading and services firms and stakeholders to predict the impact of permissible return (yields) to them since this study revealed a new knowledge on the relationship of capital structure towards trading and services sectors which is still under research in Malaysia.

As a recommendation, the outcome of the study should be able to be applied as a guideline by firms especially those who have issued debt security and the firms who have intended to issue short term or long term debt towards profitability and the change of capital structure. From the trading and services based investors, analysts and fund managers' perspective, this study will help to value add their investment decisions on the firms under scrutiny. The study will be able to help Bank Negara Malaysia and Securities Commission to monitor the development of capital structure in Malaysia.

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