Capital Structure Decisions: Evidence from Large Capitalized Companies in Malaysia

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ABSTRACT

This study aimed to determine the factors influencing the capital structure decisions in Malaysia using the companies listed on the FTSE Bursa Malaysia Top 100 Index. The objectives of this study were achieved by examining the relationship between leverage (dependent variable) and four determinants identified as independent variables, which included profitability, tangibility, liquidity and firm size. Data of 69 firms which covered the period from 2007 to 2011 were evaluated using the panel data analysis with total observations of 345 firm-years. By applying the fixed effects regression model, results showed that profitability, tangibility and liquidity had significant negative relationship with leverage while firm size is positively related with leverage. Moreover, results also revealed that profitability was the most influential factor of the capital structure in Malaysia. The findings of this study were consistent with several previous studies as well as the theoretical background of capital structure determinants. These results also may represent the unique characteristics of capital structure of firms in Malaysia.

Keywords: Capital Structure, Bursa Malaysia FTSE 100 Index, Pecking Order Theory, Panel Data
1. Introduction

Issues on credit expansion have been widely debated and became an issue of concern since the last 40 years. Many firms have struggled with strong capital structures over the past four decades and often failed to make sufficient liquidity to survive in the unavoidable contractions during the credit expansion cycles. Financially, capital structure means the way firms’ asset being financed through the combination of equity, debt, or hybrid securities. In short, it is a mixture of company’s debts, common and preferred equity (San and Heng, 2011). In the modern business context, capital structure is vital and crucial in financial management of a firm. This is because capital structure provides insight of a firm’s risks. A highly levered firm is a firm that possesses higher level of debt. Thus, the highly levered firm has much greater risk compared to firms with lower level of debt. In addition, major misjudgment in financing may cause financial distress, liquidation and bankruptcy. When firms are not able to service debt, firms would face costs of financial distress (Pandey, 2004). Therefore, highly leveraged firms have to allocate an efficient mixture of debt and equity for the firm’s capital in order to reduce cost. The financial managers play a very important role in achieving the best capital structure to maintain the firms in the industry. Financial managers would have to minimize financial costs and maximize shareholders’ wealth by deciding the best debt-to-equity ratio. This is to relieve potential pressures on the firm’s long-term financing. To decide the appropriate level of borrowing, it would be essential to know whether changing of debt and equity ratio would increase the shareholders’ wealth (Mahmood et al., 2011).

Since the introduction of MM theory, capital structure has been a popular research topic in finance. Following the three theories of capital structure, many researchers have conducted research on the determinants of capital structure, especially in developed countries. There were also researches done in several developing countries such as Libya (Buferna et al., 2005), Ghana (Amidu, 2007), Saudi (Al-Ajmi et al., 2009), Egypt and Pakistan (Afza and Hussain, 2011). Past researches on capital structure determinants were carried out under many criteria, considering different determinants as well as different sectors in the country. Most studies in capital structure determinants have only been conducted in specific sectors or countries. Different countries have unique characteristics such as environment and regulation that govern the firm’s activities. As a result of that, findings on the capital structure studied in the past were mixed and inconsistent. Moreover, many studies had been done on firms in major developed countries, especially in the USA and there were lack of attention that has been paid to other developing countries. Thus, there was little understanding of the capital structure determinants of firms outside the USA, other major developed as well as a few developing countries (Al-Ajmi et al., 2009).

From the research by Deesomsak et al. (2004), it was stated that debt and equity choice depends on the firm’s characteristics. Therefore, often it is difficult to interpret the empirical evidence without a proper methodology. In view of the fact that, choice of debt and equity depends on characteristics for firms, research should be done in countries and sectors with different characteristics. Results from a specific research cannot be used to generalize and used for specific countries and sectors. Similar to Al-Ajmi et. al. (2009)’s justification, Deesomsak et al. (2004) also mentioned that there were still little that understood the firms’ financing mix determinants outside the USA as well as other major developed countries. In addition, there were only few and most of the researches on the impact of capital structure on firm performance were done in developed economies on large and listed firms. Ooi (1999) revealed that several studies have been carried out for capital structure of firms in different sectors of the economy, namely manufacturing firms, electric-utility firms, non-profit hospitals and agricultural firms. There were also many other sectors and countries that were taken into investigation of the capital structure of firms. However, how firms choose their capital structure and the factors influencing the corporate financial decision still remains unclear (Ooi, 1999). Mahmood and Mat Kila (2008) also stated that there are no specific guidelines to assist managers to make the right financial decisions since the factors were still unclear. Adding to that, Al-Ajmi et. al. (2009) uttered that understanding of the factors influencing the finance decisions have yet to be found.

Limited research was conducted outside of USA and other major developed countries (Al-Ajmi et. al., 2009). Countries with different environment have different factors influencing the capital structure
decisions, thus financial decisions cannot be made based on the results from the researches done in other countries. Moreover, there are only few researches done on capital structure determinants in Malaysia and only covered several sectors. For instance, Pandey (2004) found a saucer-shape relationship between profitability and capital structure in Malaysia due to agency costs, costs of external financing and interest. From the research conducted by Mahmood and Mat Kila (2008), results showed that Malaysian firms have unique characteristics. However, the sample size of the research was too small, whereby only 17 companies were taken into consideration. Hence, results from the research cannot represent the characteristics of Malaysian firms. Additionally, Pratomo and Ismail (2006) conducted their research on capital structure focusing only in the Islamic bank performance. On the other hand, Mahmood et. al (2011) had focused on the property sector in their research. Results implied that firms in the property sector usually rely heavily on external funding to support their investment activities. Also, results suggested that capital structure in the property sector cannot be entirely explained by the specific determinants. Besides that, the research that was carried out by Mahmood and Zakariya (2007) was also limited to the property and construction sectors only. In the Malaysian trading and services sector, Jamal et. al (2011) highlighted that growth opportunities, liquidity and tangibility influence firms’ financing decisions. Profitability and firm size however, does not appear to have any significant effect on their capital structure decision. Therefore, existing results cannot be used to make financial decisions since there is insufficient evidence to show the relationship between the factors influencing the capital structure decisions in Malaysian firms. Based on these findings, it can be concluded that capital structure decisions were limited to specific sectors thus cannot represent the capital structure of the overall firms in Malaysia since firms in different sectors have different firm characteristics.

This study differs from previous studies as this study was not limited to specific sectors in Malaysia. Also, some previous studies covered a limited number of firms only. This study covered the FTSE Bursa Malaysia 'Top 100 Index, which are large capitalized firms in Malaysia and hence, this study was significant to represent the large firms in Malaysia. Besides, this study utilizes new approach in the analysis by using panel data regression analysis (based on balanced panel data set with fixed effect model) to find the capital structure determinants. Lastly a more recent data set covering the 2007 to 2011 period is used, thus allowing for a more relevant and up-to-date findings.

1.1 Objective of Study
The overall objective of the study is to examine the determinants of capital structure in Malaysia, using companies listed on the FTSE Bursa Malaysia Top 100 Index.

2. Literature Review

2.1 Origin of Capital Structure
The modern revolution of capital structure theory was started by Franco Modigliani and Merton Miller in 1958. This theory is also known as the MM theory. Modigliani and Miller (1958) revealed that under perfect or frictionless capital market condition, whereby there is no tax, transaction costs, bankruptcy costs and assets trade restrictions, the firm’s financial decisions or capital structure is completely independent of the firm’s market value. The first proposition stated that under certain conditions, a firm’s debt-to-equity ratio does not affect the market value or average cost of capital of any entity. The second proposition affirmed that a firm’s leverage does not affect its weighted cost of capital while the third proposition asserted that the firm’s market value is independent of its dividend policy. The assumptions of the MM theory were irrelevant to the real world. Hence, the theory was also broadly known as the capital structure irrelevance theory. Despite the fact that some of the assumptions are unrealistic, the MM theory is still important as the theory that provides indication on what is required to make capital structure relevant and affect the value of firms (Brigham et al., 2010). The MM theory is the beginning of the modern capital structure research that also leads to more realistic capital structure theories. Some of the more realistic theories are as discussed in the following section.
2.2 Theories of Optimal Capital Structure
The following sections review the four most important but conflicting theories of optimal capital structure that have been developed following the pioneering work of Modigliani and Miller (1958). The theories include the tradeoff theory, signaling theory, pecking order theory and agency costs theory.

2.2.1 Static Tradeoff Theory
According to Modigliani and Miller (1963), since the interest on debt was tax deductible, a firm will take 100 percent of debt for its capital structure while enjoying tax advantage. The tradeoff theory originated from the debate over the MM theory. When corporate tax was added to the original MM irrelevance theory, a benefit for debt, which was to shield earnings from taxes, was observed. This theory revealed that tax deductibility of interest payment indirectly induce a firm to borrow to a point whereby the present value of interest tax shield is offset by the cost of financial distress or bankruptcy. In other words, optimal capital structure is obtained by balancing the tax advantage of debt financing and leverage related costs. Myers (1984) mentioned that firms adopting the tradeoff theory always set a target debt ratio and gradually move towards achieving it. This theory was identified by Myers (1984) as the static tradeoff theory. The static tradeoff theory suggested that higher profitability firms have higher target debt ratio and the firms will be able to service more debt without risking financial distress. Higher profitability firms necessitate a higher target debt ratio to ensure higher tax savings from debt, lower probability of bankruptcy and higher over-investment. This theory contradicts the pecking order theory, which suggested higher profitability firms have lesser debt.

2.2.2 Signaling Theory
Signaling theory was introduced by Ross (1977) who concluded a positive relationship between profitability and leverage, which also contradicts the pecking order theory. The fundamental idea of the theory is that the capital structure decisions signals outside investors the information of the insiders. In other words, managers in the firms know the true distribution of the firms’ returns but the investors do not. The term “signal” in this theory refers to the action taken by a firm’s management to provide indication to the investors about how the management examines the firm’s prospects (Brigham et al., 2010). The managers would be more relax with equity than debt because if the firms go bankrupt, managers might lose their jobs. If managers keep increasing debt for the firms’ capital structure, it reflects a signal of higher future cash flow and the confidence of managers toward the firms. Consequently, investors would take the high level of debt as a signal of “higher quality” and hence, profitability is expected to be related to leverage. Modigliani and Miller (1958) assumed that managers and investors have the same information of a firm’s prospects. This assumption is called the symmetric information. However, the truth is managers usually know and possess more private information about the firm’s operations and investment opportunities compared to the investors. In other words, there exists imbalance information between the company and the public. It is identified as the asymmetric information. Due to the miscommunication between the company and the public, when firms have fewer tangible assets, the public would perceive that the firms are of low value. As a result, potential investors will reduce their interest in investing in firms that have been perceived as low valued firms.

2.2.3 Pecking Order Theory
The theory has been developed by Myers and Majluf (1984). They stated that firms should be following a hierarchical order of financing decisions when it comes to the choice of capital structure by considering their financial benefits. This theory was constructed and designed to limit inefficiencies of the asymmetric information theory. Any issuance of debt or equity is thought to be generating a signaling effect to the investors, where the firms are presumed to be doing well when the firms are buying back their shares and vice versa. Therefore, the pecking order theory supports that the firm will tend to use internal funds because informational problems can be avoided since internal funds are of low risks, less sensitive to
mispricing and valuation errors. However, if internal funds are inadequate or depleted, the firms will be financed using external funds with debt by benefiting the market trust towards them if they have good sales. Following this theory, equity or issuance of firm’s shares will be the last resort in the choice of capital structure of the firms. According to the law of lease effort or resistance, internal financing is more preferable compared to external financing and the firm will only consider equity when the firm’s debt capacity is at maximum level. Myers (1984) affirmed that firms will issue safest security, which is debt then only equity financing as the firms seek more external financing, it will go down the pecking order of securities, safe to risky debt to convertibles and equity for the last. Thus, the pecking order theory implies the existence of a financing hierarchy with first the internal funds, followed by debt and lastly equity. The reason for the hierarchical order is that internal funds are regarded as ‘cheap’ and not subject to any external interference. External debt is ranked second because it is observed cheaper and has fewer restrictions compared to equity. Lastly, equity is viewed as the most expensive and dangerous since it can lead to potential loss of control of the firm. Furthermore, Myers (1984) also mentioned that there are no well-defined target debt ratios but the ratios only change when there are imbalances of internal cash flow, net of dividends and the real investment opportunities arise. Therefore, in this theory, it is found that highly profitable firms with limited investment opportunities have low debt ratio and vice versa.

### 2.2.4 Agency Costs Theory

Jensen and Meckling (1976) introduced the agency costs theory. The agency costs arise due to the conflict of interest between shareholders and debt holders. Firms with high growth opportunities had more agency costs problems (Myers, 1977). This theory considered debt as an important factor that reduces conflict between managers and shareholders. The separation of management and ownership in a firm causes the agency costs. Since management and shareholders attempt to act in their own interests, managers might make financing decisions that are not in line with the goal of maximization of shareholders’ wealth. Therefore, it is vital to determine the level of debt in the capital structure of firms so as to avoid or reduce conflicts within the firms. Debt together with the interest payments will be able to reduce the agency costs between managers and shareholders (Buferna, 2005). This is because managers would be concerned about losing their job and hence, they tend to manage the firm as efficiently as possible so as to meet the interest payments, thus in line with the goal of maximization of shareholders’ wealth. This can be supported by Myers (2001) who pointed out that unless the managers are also the owners of the firms, otherwise the managers will not bear full costs that managerial actions impose on investors. Also, there is no pure, apparent measure of managers’ performance. Teh et al. (2012) stated that the agency costs problems also exist due to the resolution between ownership and control of the firm. Managers have incentives to cause their firms to grow beyond the optimal size. Growth increases managers’ power by increasing the resources under their control. Jensen and Meckling (1976) recommended that given increasing agency costs between debt and equity holders, there would be optimum combination of outside debt and equity to reduce total agency costs.

### 2.3 Empirical Studies on Determinants of Capital Structure

In a recent study, Faris Mouamer (2011) tested the explanatory power of capital structure models in Palestine using a total of 15 firms for the period from 2000 through 2004. The variables used were leverage ratios, profitability, liquidity, age of firm, asset structure firm size and sales growth for the panel data methodology that involves pooling of observations on a cross-section of units over several times. From the research, relationship between assets’ tangibility and total debt were positive but insignificant. Liquidity was found to be significantly negative with short-term debt, indicating that firms with higher liquidity pay off short-term debts using the liquid assets. Growth opportunities is negatively related to long-term debt and passively related to short-term debt. Findings signified that short-term debts are converted to long-term debts with the ability of firms to roll over short-term debt. Fixed assets and long-term debt were positively related while short-term debt otherwise. Finally, size was found to have positive
relationship with long-term debt and negative relationship with short-term debt. Results explained that large firms have opportunity to borrow in the long-term whereas small firms remained using short-term financing.

Afza and Hussain (2011) performed a research on the industry specific attributes of automobile sector affecting the capital structure decisions. Panel data regression, which was also known as constant coefficient model was used in the research alongside 22 out of 26 firms of automobile sector in Pakistan over the period between 2003 and 2007. The model utilized leverage as the dependent variable and tangibility of assets, firm size, profitability, tax provision, non-debt tax shield liquidity and cost of debt as the independent variables. From the research, tangibility was positively influencing leverage but insignificant. The relationship reflected firms with large asset structure favor debt financing to benefit from tax shield, supporting the static tradeoff theory. On the other hand, results showed that the relationship between profitability and leverage was significantly negative. It was analyzed and concluded that profitable firms in the automobile sector financed their investments following the pecking order theory by using retained earnings first and then followed by debt and finally equity. Leverage and taxes have significant positive relationship while leverage and non-debt tax shield have insignificant negative relationship. Liquid firms prefer internal finance in financing their investments and were in line with the pecking order theory. The relationship between leverage and cost of debt, which was insignificantly negative, indicated that firms with high cost of debt avoid debt financing. This was consistent with the static tradeoff theory. Size was positively related to leverage signified that large automobile firms opt for debt financing since bankruptcy cost was only a small portion of the firms’ value and hence, less prone to financial distress.

Qiu and La (2010) reinvestigated what influenced some firm characteristics have on Australian firms’ capital structures. Panel regression was employed for the annual data for a cross-section listed Australian firms during the period between 1992 and 2006. Data consist of 65 firms in 1992 and 412 firms in 2006. In the research, the dependent variable was debt ratio while firm size, asset tangibility, profitability, growth and firm risk were used as the independent variables. Results from the research showed that firm size and debt ratio was insignificantly related. On the other hand, debt ratio increases with asset tangibility but decreases with the other three independent variables. The negative relationship between debt ratio and profitability indicated that pecking order theory is more relevant in Australia compared to the tradeoff theory. It was also mentioned that the negative impacts of profitability, growth prospects and firm risk were significant and in line with bankruptcy costs, signaling effect as well as the agency costs theories. Results in this research were in contrast with Deesomsak et al. (2004) who concluded that risk, profitability and growth do not significantly affect capital structure in Australia. This research signified that profitable firms are more concerned about agency costs while unprofitable firms are more concerned about bankruptcy costs in decision making of capital structure. Also, bankruptcy costs, agency costs, signaling effects and issuance cost of equities are the main concerns of Australian firms’ capital structure decisions.

Al-Ajmi et. al. (2009) performed a research on capital structure decisions in a Zakat environment with Riba prohibition in Saudi Arabia. Final sample comprises 53 firms that cover period from year 2003 to 2007 for the panel data methodology. The dependent variable, leverage ratio was measured as debt ratio, short-term debt and long-term debt. Independent variables were profitability, size, growth, tangibility, ownership structure, risk, dividend payment and liquidity. It has been identified that majority of the Saudi firms depend more on short-term debt compared to long-term debt. The negative correlation between profitability and leverage measures was consistent with the pecking order theory implying that firms prefer to use internal profits to finance investments. Size was found to be a significant determinant for all leverage measures because larger firms face lower bankruptcy risk and it is easier to get loan from banks. Following the pecking order theory, growth was positively related to leverage. Tangibility was significantly negative for debt ratio and long-term debt and insignificant for short-term debt. It was explained that firms do not finance long-term asset with long-term debt. As for the ownership structure, it was found that leverage was significantly negative for government ownership, significantly positive for institutional ownership and insignificantly negative for family ownership. Furthermore, consistent with the
financial distress theory, risks negatively influence leverage. It was explicated that firms with high volatility earnings have higher risk of being unable to meet their debt commitments. The relationship between dividend payment and leverage was significantly negative, consistent with the pecking order theory. Liquidity was also significantly negative and in line with pecking order theory as well as static tradeoff theory. The research concluded that leverage is positively related to profitability, size, growth opportunities and institutional ownership and negatively related to tangibility, government ownership, family ownership, business risk, dividend payments and liquidity.

Abor and Biekpe (2009) examined the capital structure determinants of small and medium enterprises (SMEs) in Ghana from year 1998-2003. The sample utilized consists of 160 SMEs and the Prais-Winsten regression model was employed. The proxy used for capital structure in the research was long-term debt and short-term debt. Explanatory variables include firm age, firm size, asset structure, growth, profitability and firm risk. Results demonstrated that firm age was positively related to long-term debt and negatively related to short-term debt. The findings showed that older firms have better credit history and hence easier to access debt compared to newer firms. Firm size, which is positively related to long-term debt ratio implied that larger firms are more diversified and are perceived to have lower risk. Asset structure and long-term debt has significant positive relationship. The relationship showed that small firms are perceived as risky ventures and small firms usually need to be more collateral when accessing long-term debt. In contrast, asset structure and short-term debt has inverse relationship. Profitability and both debt ratios have relationships that are consistent with the pecking order theory, showed that less profitable firms require more external debts than more profitable firms. Growth and long-term debt are positively related while growth and short-term debt are negatively related. Finally, the relationship between risk and both debts were negative but statistically insignificant. Abor and Biekpe (2009) concluded that short-term debt was found relevant and vital in representing the financial sources for SMEs in Ghana. However, SMEs in Ghana also need long-term debt to finance the growth of firms. Furthermore, this study evidently supported the pecking order theory, implying that more profitable firms employ less debt in their capital structure decisions.

De Jong et al. (2008) conducted a research on capital structure around the world, which analyzed the importance of firm-specific and country-specific factors in the leverage choice of firms. The period between 1997 and 2001 were considered in the study. The sample comprised of 11845 firms from 42 countries, which are equally divided between developed and developing countries. Leverage was employed as the dependent variable in the research. The firm-specific leverage determinants were tangibility, business risk, firm size, tax rate, growth opportunity, profitability and liquidity while the country-specific leverage determinants were legal enforcement, shareholder or creditor right protection, market or bank-based financial system, stock or bond market development and growth are in a country’s gross domestic product (GDP). For the firm-specific leverage determinants, the ordinary-least-square regressions were employed whereas the simple pooled OLS regressions were used for the country-specific leverage determinants. Researchers found that firm-specific leverage determinants differ across countries but previous researches assume equal impact of these determinants. Secondly, researchers pointed out that even though there is conventional direct impact of country-specific factors on the firms’ capital structure, there is also indirect impact because country-specific factors also influence the roles of firm-specific leverage determinants.

Al-Najjar and Taylor (2008) investigated the relationship between capital structure and ownership structure in an emerging market using a sample of 86 non-financial Jordanian firms. The research applied the economics modeling using both single equation and reduces equation models for panel data. The dependent variable used was leverage or total debt ratio while the independent variables were dividend per earnings ratio, profitability, business risk, tangibility, liquidity, growth rate and firm size. From the results of the research, dividend per earnings ratio had no significant relationship with leverage. There was no relationship between institutional ownership and dividend per earnings ratio as well. Hence, there is no confirmation that investors would consider the dividend per earnings ratio when making capital structure decisions. Profitability and leverage has negative relationship, which is consistent with the pecking order theory. However, there is limited support that investors would consider profitability when making capital
structure decisions. Business risk and debt ratio were negatively related. It implied that firms with volatile incomes are liable to use less debt and it supports the bankruptcy costs theory. Also, business risk and institutional ownership were negatively related. This is because investors would choose to invest in lower risk firms as higher risk firms are more prone to bankruptcy. As for tangibility, results showed positive relationship with leverage, following the agency costs theory. The negative relationship of tangibility with institutional ownership implied that investors consider tangible assets as an indication of debt capacity and since investors would prefer to invest in less debt firms, hence investors would choose to invest in firms with less tangible assets. Liquidity is positively associated with firm’ debt and liquidity of firms is also positively related to institutional ownership. Investors consider high liquidity firms are more capable of paying obligations and also face lower risk. Growth rate was found to be significantly positive with leverage. This contradicts the agency theory as Jordanian firms with high growth rate finance investments using debt. In addition, the relationship between firms’ growth and ownership structure was also positive. It signified that high growth firms are more beneficial to investors than low growth firms. The last independent variable, size is significantly positive with leverage. This meant that large Jordanian firms are less susceptible to bankruptcy. The positive relationship between firm size and ownership structure showed that large firms have the resources and are able to minimize risks, hence less vulnerable to bankruptcy. Al-Najjar and Taylor (2008) concluded that Jordanian firms adapted the same determinants of capital structure as the developed market. Moreover, results indicated that tangibility, size of firm, growth rate and business risk were considered as the joint determinants of capital structure and institutional ownership.

Eldomiaty (2007) studied the determinants of corporate capital structure in emerging economy. The aim of the study was to examine to which extend capital structure decisions are affected by the tradeoff theory, pecking order theory and free cash flow theory. This study covered data of 99 firms from 14 non-financial industries. The dependent variable in this study, which was debt ratio was divided into short-term and long-term debt. The independent variables used for the tradeoff theory were target debt ratio, average industry leverage, structure of tangible assets, relative tax effects and bankruptcy risk. Results of the study were demonstrated according to the three theories. As postulated in the tradeoff theory, long-term debt and the ratio of debt to equity are positive and significant, implying that corporate leverage adjusts positively according to the long-term debt changes. It was pointed out that firms may increase debt in order to benefit from tax savings since the effective corporate tax rate was found to be significantly positive. Negative coefficient of the bankruptcy risk implied that firms reduce leverage to pass up higher degrees of bankruptcy risk. In accordance to the pecking order theory, long-term debt was examined to be positive and significant, showing that corporate leverage adjusts positively according to the long-term debt changes. The negative and significant coefficient of growth, operating income and return on investments were in line with the pecking order theory. In contrast, sales growth was positive and significant and not in line with the pecking order theory. Also, significant positive coefficient of PE ratio showed the when the PE ratio is increasing, firms increase leverage instead of issuing equity. As for the free cash flow theory, short-term debt was significantly positive, showing that corporate leverage adjusts positively according to the short-term debt changes. Significant negative coefficient of interests rates implied that firms borrow when interest rates is low. One of the three cash flow related variables present in the model indicated that assumption of the free cash flow theory do not have effect on the borrowing decisions. On the whole, results demonstrated that the independent variables in the regression equation were significantly high. Therefore, the construction of model was quite indicative. The study concluded that the tradeoff theory and pecking order theory have a great impact on the capital structure decisions. This meant that achieving optimal capital structure is not one way to go and the theories do not present a complete explanation of the financing decisions.

Seppa (2008) conducted a research to examine the relationship between company-specific factors and capital structure decisions as well as the behavioral differences different sizes of firms. The sample of 260 Estonian non-financial firms was categorized into small, medium and larger firms. Debt was used as the independent variable. The explanatory variables were amortization, earnings before interest and taxes, return on investment, tangibility, net working assets and business size. From the research, it was found
that tangibility was significantly positive related to debt and the business size was weakly related with debt. Significant and negative correlation was found between return on investment and debt. For business risk, it was found that it has weak correlation with debt but only for small firms. Results showed that the Estonian non-financial firms follow the pecking order theory in their capital structure decisions. Hence, there was insufficient evidence to support the optimal capital structure decisions in the long run. Additionally, behavioral patterns differ between small and large firms. However, the differences were still unclear.

Song (2005) conducted an empirical study to examine the determinants of capital structure and debt level for about 6000 Swedish based firms during the period from 1992 to 2000. Determinants included in the study were tangibility, non-debt tax shield, profitability, size, expected growth uniqueness and income variability. Panel data regression was employed to examine the determinants affecting the three leverage measures, which are total debt ratio, short-term debt ratio and long-term debt ratio. Tangibility was found to have positive relationship with total and long-term debt and negative relationship with short-term debt ratio. Non-debt tax shield has no correlation with total debt ratio, positive correlation with short-term debt ratio and negative correlation with long-term debt ratio. This revealed that when firms are engaged in tax shelter schemes, firms will mostly consider long-term debt. In line with pecking order theory, profitability in this study was found to be negatively correlated with all leverage measures. The relationship between size and long-term debt was negative whereas short-term debt and total debt were positively related to size. Results showed that small firms are supply constrained and therefore, small firms are unable to employ long-term debt financing. There was no relationship between leverage with expected growth as well as uniqueness. The income variability and leverage relationship was almost zero but statistically significant.

Deesomsak et al. (2004) carried out a research to investigate the determinants of capital structure of firms operating in the Asia Pacific region. The four countries with different legal, financial and institutional environments, which were included in the research were Thailand, Malaysia, Singapore and Australia. The samples used in this research include all non-financial firms listed in the relevant national stock exchanges, which consist of 294 Thai, 669 Malaysian, 345 Singaporean and 219 Australian firms for the period 1993 to 2001. The research was done using the Ordinary Least Square (OLS) for each country. The dependent variable was leverage while the explanatory variables were tangibility, profitability, firm size, growth opportunities, non-debt tax shield, liquidity, earnings volatility and share price performance. The results from this research showed that leverage and tangibility is positively related as postulated and is significant for all countries except Australia. The insignificant effect was explained by the tight family held and concentrated ownership as well as the close relationship between firms and lenders. Therefore, in order for the Australian firms to borrow, less collateral would be required. Profitability and leverage was found to be negative but only significant for Malaysian firms. The negative relationship between profitability and leverage in Malaysia is consistent with the pecking order theory that stated that firms prefer internal finance when profits are high. Except Singapore, the firm size in the other three countries showed positive significant impact on leverage. Results were in line with the agency costs theory, which is larger firms have high debt level relative to small firms. The negative relationship for firm size in Singapore was explained by the Singapore firms receiving government support. Consequently, regardless of the firm size, Singaporean firms face less risk of financial distress. Supporting the tax-based models of capital structure, the non-debt tax shield revealed the negative relationship with leverage for all countries. Liquidity and share price performance were found to be significantly negative with leverage for all countries. These illustrated that firms tend to use their liquid assets to finance their investments than to use debt. Also, firms tend to prefer equity relative to debt when share prices are at rise. Lastly, there was no significant effect between earnings volatility and leverage in any of the four countries. Researchers clarified that firms may disregard the earnings volatility if the risks and costs of entering into liquidation are low. It was concluded that there are some significant differences between countries. Therefore, capital structure decision is not only affected by the firms’ own characteristics but also the corporate governance, legal framework and institutional environment of countries in which the firm operates.
Chen (2004) investigated the capital structure determinants of 77 Chinese public-listed companies using the panel data method for period between 1995 and 2000. The research involved total leverage and long-term leverage as the dependent variables and profitability, size, growth opportunities, tangibility, earnings volatility and non-debt tax shield as the independent variables. Profitability was found to be in line with the pecking order theory as it was negatively related to leverage in Chinese firms. Also, the negative relationship contributed to pass up underinvestment problems and new projects being mispriced. The relationship between growth opportunities and leverage was positive. Tangibility was also positively related to leverage, particularly long-term leverage. This relationship was in line with both the tradeoff and pecking order theory. As for firm size and total debt, insignificant positive relationship was determined while significant negative relationship was determined for long-term debt. This implied that large firms have more access to the capital markets for equity due to the reputation in the market. The research reflected that some modern capital structure theory insights in developed countries are also pertinent to China. However, the capital structure decisions of the Chinese firms followed a new pecking order theory, with retained profit first, followed by equity before long-term debt. This was due to the fundamental assumptions proposed in research in the western countries are not valid in China. Last but not least, the factors influencing the Chinese banking firms’ capital structure decisions include institutional differences and financial constraints.

Booth et al. (2001) carried out a study to analyze the capital structure choices of firms in ten developing countries. Data covered a maximum of 100 largest public listed firms in each country from 1980 to 1990. The developing countries were India, Pakistan, Thailand, Malaysia, Turkey, Zimbabwe, Mexico, Brazil, Jordan and Korea. Simple pooling and fixed-effect model were used as the method of analysis. The dependent variable, debt ratio were divided into three, which are total debt ratio, long-term book-debt ratio and long-term market-debt ratio. Tax rate, business risk, asset tangibility, size, return on assets, market-to-book ratio were the firm-specific variables employed while stock market value, liquid liabilities, real GDP growth rate, inflation rate and Miller tax term were the macroeconomic variables used. Researchers realized that determinants relevant to the capital structures of United States and European countries were also relevant to the capital structure of developing countries. Researchers found that knowing the determinants help to predict the firms’ financial structure better than knowing only its nationality. Likewise, researchers also found consistent results in both the pooled data and country results. Findings showed that more profitable firms employ less debt and were in line with the pecking order theory as well as supporting the asymmetric information theory. Therefore, researchers concluded that external financing is more costly, hence firms would opt for internal finance in their capital structure decisions.

Ooi (1999) studied the financial structure of property companies in the UK. The main source of data was from DATASTREAM, which consists of 100 UK property companies between 1989 and 1996. Panel data that involved pooling of observations on cross-section of units over several time periods was also used in this research. Results from the research demonstrated that property asset intensity ratio, trading activity, development undertaking, company size, systematic risk, interest rate and market condition were significant while growth rate, profitability and tax rate were not significant. Asset structure was found to be an essential capital structure determinant of property companies, showing that companies with higher property asset intensity utilize more debt financing. The negative relationship between growth rate and debt confirmed larger proportion of firms’ value accounted by growth opportunities apply less debt financing. Total debt ratio and level of property trading were positively related. Systematic risk was inversely related to total debt ratio as predicted. Opposing the tradeoff theory, the significant positive relationship between development activity and leverage implied that companies with heavy commitments in property development occupy more debt financing. Also, inverse relationship between firm size and leverage was in contrast with the tradeoff theory. Results proved that smaller property companies rely more on bank loans since there are not much choices. When interest rates are low, property companies employ more debt. Debt ratio of property market increases in a declining property market. Taxation was identified playing a minor role in capital structure. Last of all, corporate profitability was insignificant with leverage. Therefore, the finding was unable to support the pecking order theory on the relationship.
between corporate performance and leverage. Results from the research can conclude that property companies generally rely heavily on external funding for investments. Financial risk considerations in debt financing or property companies were also determined to be significant. Finally, underlying market sentiment and interest rates were considered by financial managers of the property companies when making financial decisions.

Wiwattanakantang (1999) studied on the capital structure determinants of Thai firms in 1996. Sample of study comprise 270 listed Thai firms. Ten dummy variables were used to represent the 10 industries involved in the study. The other explanatory variables were non-debt tax shield, tangibility, profitability, business risk and firm size. The agency costs variable, namely types of firms, family-owned, conglomerate groups, foreign owned firms, state owned firms were represented by the dummy variables, with 1 or 0 depending on their existence. As for the dependent variable, two leverage ratios were utilized, which are book value of total debt divided by total assets and book value of total debt divided by the book value of total liabilities plus market value of total equity. Results from the study demonstrated that non-debt tax shield, tangibility, profitability and growth were significant and as postulated sign. Therefore, results from the Thai firms were found to be similar to the developed countries. Furthermore, the managerial ownership appeared to have positive and significant relationship with leverage for both the directors and CEO involvement. Firms with different types of controlling shareholders seemed to have different capital structure decisions. For instance, single family owned firms have higher debt levels compared to other firm types. In addition, factors related to governance mechanisms of Thai firms also affect the capital structure decisions. Finally, firm age was not significantly related to leverage in Thai firms.

In the Malaysian context itself, Mahmood and Kila (2008) conducted research on the determinants of capital structure for firms listed in Bursa Malaysia during the period between 2000 and 2005. The data in the research was derived from financial statements of 17 companies with a total of 102 observations. The dependent variable employed was total debt ratio while the independent variables were size of firm, liquidity of firm and interest coverage ratio. By combining the cross-sectional data with time series data, the pooled OLS estimations were applied in the research. Results from the research showed that the size of firm, liquidity of firms and interest coverage ratio were significantly negative with total debt ratio. The negative relationship between size of firm and total implied that larger firms are less dependent on debt financing compared to smaller firms. As for liquidity of firms, it was indicated that firms with high liquidity tend to use less debt and finance their investments following the pecking order theory. The researchers pointed out that large firms are able to generate high cash inflows and hence able to finance their investments using the internal earnings. Since firms use their internal earnings to finance their investments, less leverage employed in the capital structure, hence the interest coverage ratio was negatively correlated with total debt ratio. In the research, the relationship between growth of firms and capital structure was insignificantly negative. Finally, the results of dummy variable show that there is significant difference in capital structure among the firms that adopt more debt (more than 30 percent of their total assets) and firms that employ less debt financing.

Pratomo and Ismail (2006) on the other hand, performed a research on Islamic bank performance and capital structure in Malaysia. The aim of the research was to identify the presence of agency costs in the banking literature. Samples comprised 15 Islamic banks in Malaysia from 1997 until 2004. Unit root test was employed to test the stationary of data along with fixed effect model as the representative model in the research. The dependent variable used was bank’s profit efficiency and the independent variables were capital to asset ratio, standard deviation of return on equity, size of company, total loan, bank’s investment in securities and deposit Herfindahl index of local market concentration. The results demonstrated that highly levered banks are better than low or unlevered banks. The capital to asset ratio showed a negative sign, hence it was revealed that the higher the capital of a bank, the lower its efficiency or performance. Results for total loan and bank’s investment in securities were insignificantly negative, suggesting that there is a caution of bank performance. Conversely, the positive relationship between size and the bank’s profit efficiency explained that banks with larger assets tend to achieve higher
performance. Findings from the research were in line with the agency costs theory, which stated that the higher leverage or the lower equity is associated with higher profit efficiency. In addition, findings that size of bank is negatively related to bank’s performance support the postulation that large firms tend to be unlevered.

2.4 Dependent Variable
The central issue of capital structure relied on the amount of debt use by the firm to finance its assets, which further known as financial leverage. When financial leverage increases, return on investment for shareholders would be higher. However, Jensen and Meckling (1976) stated that there would also be increasing causes of financial distress and agency costs. It is argued that agency costs in corporate finance is unavoidable and play a vital role in financing decisions due to conflicts. The agency theory employed debt as a necessary factor that creates the conflict between equity holders and the managers. The agency costs theory stated that managers usually act in their personal interests while seeking higher than market salaries, privileges, job security and sometimes even direct capture of assets or cash flows. In other words, managers usually overspend or take less leverage to avoid risks of losing job, reputation and wealth. This is seen to be a detriment to the firms’ shareholders. Besides, Myers (1984) pointed out that the manager will not bear the full costs of managerial actions impose on investors unless that he or she is the owner-manager. Furthermore, there is no pure, apparent measure of the managers’ performance. However, debt together with payments of interest would be able to reduce the conflicts between investors and managers (Bufferna et al., 2005). Additionally, Myers (1984) also uttered that agency costs may also occur because of the conflicts between debt and equity investors. Hence, financial leverage is significant in reducing the agency costs since Jensen and Meckling (1976) suggested that there would be an optimum combination of debt and equity to reduce total agency costs. Leverage is measured as total liabilities to total assets (Rajan and Zingales, 1995).

2.5 Independent Variables
The factors affecting the capital structure decisions in a firm are the determinants of capital structure. The capital structure determinants such as profitability, tangibility, liquidity, growth opportunities and firm size will be discussed in the following sections.

2.5.1 Profitability
According to Myers (1984), firms prefer to finance their investments using retained earnings following the pecking order theory. According to the pecking order theory, firms have an ordered financing preference, whereby firms prefer retained earnings as their main source of financing investments, followed by debt and the last resort would be external equity financing. The amount of the retained earnings depends on the profitability of firms and profitable firms tend to use less debt than less profitable firms. The reason for firms to choose internal funds as their main source of finance was because internal funds were regarded as ‘cheap’ and not subject to any outside interference. Thus, profitable firms should have lower leverage ratio because they have more retained earnings and hence profitability is expected to be negatively correlated with leverage (Titman and Wessel, 1988; Rajan and Zingales, 1995; Booth et al., 2001). The negative relationship between profitability and leverage supported the pecking order theory and contradicted the tradeoff theory. Profitability is measured as earnings before interests and taxes (EBIT) to total assets (Booth et al., 2001; Pandey, 2004; Song, 2005; Chen, 2004; Deesomsak et al., 2004).

2.5.2 Tangibility
The agency costs can be reduced if firms have sufficient tangible assets because firms with significant tangible assets will have higher level of debt and will be less financially constrained (Jensen and Meckling, 1976). According to Harris and Raviv (1991), firms with high proportions of tangible assets are likely to have low cost of debt because the presence of tangible assets can serve as collateral against external funding. Firms that is unable to provide collateral will have to pay higher interests or will have to issue equity instead of debt. However, Pandey (2001) pointed out that some firms employed tangible
assets to generate internal funds for financing their investments. This is in line with the pecking order theory that stated that firms prefer internal finance compared to external debts. The tangibility of assets can be computed by the ratio of fixed assets to total assets (Rajan and Zingales, 1995; Pandey, 2004; Song, 2005; Abdul Jamal et al, 2011; Teker et al., 2009).

2.5.3 Liquidity
Pecking order theory proposed that firms prefer internal finance over external debt. Hence, firms with high liquid assets will be able to finance the firms’ investments with less debt. Furthermore, Deesomsak et al. (2004) pointed out that managers are able to control the liquid assets in favor of the shareholders but against the interests of the debt holders, such as investing in unprofitable projects. This would increase the agency costs of debt. Thus, it is anticipated that liquidity is negatively correlated with leverage. The ratio of current assets to current liabilities was used by Deesomsak et al. (2004) and Al-Ajmi et. al. (2009) as the proxy to examine the liquidity of firms.

2.5.4 Firm Size
Large firms are typically more diversified and less prone to bankruptcy (Rajan and Zingales, 1995). In accordance to the static tradeoff theory, some researches revealed that larger firms have greater level of diversification to reduce cash flow volatility and hence, bankruptcy risk is lower (Kouki and Said, 2012). In this case, the firm size has a positive impact on leverage (Rajan and Zingales, 1995). In the pecking order theory, considering the asymmetric information, firm size is used as the opposite measure of information attained by investors (Kouki and Said, 2012). Larger firms have lower information asymmetry and are able to issue more equity compared to small firms. In this context, leverage and the firm size have significant negative correlation (Titman and Wessel, 1988). The proxy of firm size is the natural log of assets (Pandey, 2004, Deesomsak et al., 2004; Jamal et al, 2011; Al-Ajmi et al., 2009).

3. Data and Methodology
The main sources of data for this research were the financial statements of the FTSE Bursa Malaysia Top 100 Index companies, which comprise FTSE Bursa Malaysia KLCI and FTSE Bursa Malaysia Mid 70 Index. The 100 companies cover around 81 percent of the full market capitalization of FTSE Bursa Malaysia EMAS Index. The FTSE Bursa Malaysia EMAS Index covers 93 percent of Bursa Malaysia’s Main Board (FTSE, 2009). The sample for this study covered the period from 2007 to 2011. Initially, the list of the 100 companies was obtained from the Bursa Malaysia KLSE Star Guide. However, during the process of collecting data, some companies were excluded from this study. First of all, 14 companies from the finance sector were removed from the list. This was because companies in the finance sector, for instance banks and insurance companies subject to specific rules in financing (Teker et al., 2009). Pandey (2004) also pointed out that the financial characteristics and use of leverage of firms in the finance sector were substantially different than other sectors. The financial statements of the 86 companies were downloaded from Thompson ONE Banker. Missing data were then retrieved from the companies’ annual reports, which were downloaded from the respective companies’ official website. Nonetheless, 17 companies were eliminated from this study due to data unavailability. Thus, this study focused on 69 companies listed on the Main Board of Bursa Malaysia with total of 345 numbers of observations.
To test the relationship, we developed a linear model as follows:

\[ \text{LEV}_{it} = \alpha + \beta_1 \text{PFT}_{it} + \beta_2 \text{TAN}_{it} + \beta_3 \text{LIQ}_{it} + \beta_4 \text{SIZE}_{it} + \varepsilon_{it} \]

where;
- \( \text{LEV}_{it} \) = financial leverage of firm i at time t
- \( \text{PFT}_{it} \) = profitability of firm i at time t
- \( \text{TAN}_{it} \) = tangibility of firm i at time t
- \( \text{LIQ}_{it} \) = liquidity of firm i at time t
- \( \text{SIZE}_{it} \) = firm size of firm i at time t
- \( \alpha \) = constant
- \( \beta_1 \) to \( \beta_4 \) = coefficients of independent variables
- \( \varepsilon_{it} \) = error term of firm i at time t

To analyze the determinants, panel data regression techniques were used and tested via the STATA (Version 10) computer software. According to Klevmarken (1989) in Baltagi (1995), panel data contributes several benefits. First, panel data can control individual heterogeneity which in consequence can cause misleading and biased results. It also reduces multicollinearity problems (as is often the case in time series studies) and provides more data information due to pooling individual and time dimension (in which provides more reliable parameter estimates), more data efficiency, variability and captures a better dynamic adjustments. Panel and random effect techniques are the popular tools used to estimate the panel data models. Hausman (1978) suggested that under null hypothesis, correlation should not exist between both individual effects and explanatory variables. In other words, both random and fixed effects are estimated to be consistent, with random effect are expected to be more efficient compared to fixed effects. Similar to this, Greene (1997) added that the estimates should not differ systematically under null hypothesis. While under alternative hypothesis, the explanatory variables are expected to be correlated with individual effects, that is, random effects in this case is inconsistent compared with fixed effects estimator which is said to be efficient; thus reject the null alternatives. Hausman test can be conducted to test which of these two models are the most appropriate. This study used random effect models and the results can be viewed at section 4 of the paper.

4. Empirical Result

Fixed Effect Estimation Model

Table II: Results of Hausman Test

<table>
<thead>
<tr>
<th>chi2(4)</th>
<th>92.89</th>
</tr>
</thead>
<tbody>
<tr>
<td>Prob &gt; chi2</td>
<td>0.000</td>
</tr>
</tbody>
</table>

The p-value from Table 4.3 shows that test result was significant at 1 percent significance level; hence the null hypothesis is rejected. This indicates that the random effects model is not appropriate and that the fixed effects specification model was to be preferred for the existing panel data set as the p-value is less than 0.05 for the dependent variable. Hence, the fixed effect model was used to generate statistical regression results in the following sections.
Table III: Results of Fixed Effects Regression

<table>
<thead>
<tr>
<th>Variables</th>
<th>Results</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profitability</td>
<td>0.000*** (−5.490)</td>
</tr>
<tr>
<td>Tangibility</td>
<td>0.000*** (−6.020)</td>
</tr>
<tr>
<td>Liquidity</td>
<td>0.000*** (−4.500)</td>
</tr>
<tr>
<td>Firm Size</td>
<td>0.036** (2.110)</td>
</tr>
<tr>
<td>R-Squared</td>
<td>0.258</td>
</tr>
<tr>
<td>F-Value</td>
<td>23.63 Prob &gt; F 0.000</td>
</tr>
</tbody>
</table>

*, ** and *** indicate significance at 0.10, 0.05 and 0.01 level respectively

The result suggested that all variables namely profitability, tangibility, liquidity and firm size are the main determinants of capital structure in large capitalized companies in Malaysia significant at 1 and 5 percent level, respectively. From the findings, the relationship between profitability and leverage was found to be negatively significant. The inverse relationship showed that one unit increase in profitability will decrease leverage by -0.486. The estimated t value of −5.49 (p < 0.01) was more than the critical value of t at 1 percent significance level. This indicates that just like any other firms in other countries or sectors, Malaysian firms generally prefer internal financing rather than debt financing. In other words, high profitable firms in Malaysia use more internal financing while low profitable firms in Malaysia use more debt financing because their internal funds were inadequate to finance their investments. Good profitability reduces the need for external debt. Besides, the retained profit was the fastest and easiest source of finance for most firms. The result contradicted the static tradeoff theory and was in line with the pecking order theory. This result is similar with the findings of previous studies on Malaysian property companies by Mahmood et al. (2011); Asia Pacific region (Deesomsak et al. 2004); Pakistan automobile sector (Afza and Hussain, 2011); Pakistan (Shah and Khan, 2007), Sweden (Song, 2005), Thailand (Wiwattanakantang, 1999), China (Chen, 2004), Australia (Qiu and La, 2010), Jordan (Al-Najjar and Taylor, 2008) and SMEs in sub-Saharan Africa (Abor and Biekpe, 2009).

Tangibility has significantly negative relationship with leverage at 1 percent significance level with the t value of −6.02 (p < 0.01). The coefficient of tangibility showed that one unit of increase in tangibility decreases the leverage by -0.415. Some of the previous studies such as the study by Deesomsak et al. (2004) as well as Rajan and Zingales (1995) showed significantly positive relationship between tangibility and leverage because firm’s tangible assets serve as collateral for the firms to obtain external funding. This was in contrast with the negative relationship between tangibility and leverage of Malaysian firms as analyzed in this study. The negative relationship showed that firms in Malaysia tend to use their tangible assets to generate internal funds for financing investments instead of using tangible assets as collateral to seek external funding. Some examples of tangible assets that can be used to generate more income for the firms would be the plants and equipments. With the existing equipments, a firm would maximize its usage to produce more valuable outputs. Produced outputs were the source of earnings and internal funds. These firms generally opt for internal financing rather than external borrowings and thus in line with the pecking order theory. This can be further explained and supported by the compliance to
agency cost theory. According to the agency cost theory, the use of secured debt might reduce the agency cost of debt. If the firm’s level of tangible assets is low, the manager in the firms may tend to choose a high level of debt to mitigate equity agency costs for monitoring purposes. The agency costs of debt serves as a combination of the static tradeoff theory and the pecking order theory (Ebrahim and Mathur, 2000). Nonetheless, the Malaysian firms still use debt financing but probably not the main choice of financing their investments. Therefore, the relationship was found to be negative. The inverse relationship of tangibility and leverage was also supported by some other studies done in Libya (Buferna et al., 2005), Ghana (Mohammed Amidu, 2007) and Saudi Arabia (Al-Ajmi et. al., 2009).

Negative relationship between liquidity and leverage was determined and the result showed that one unit increase in liquidity decreases -0.317 unit of leverage. The estimated t value of -4.50 (p < 0.01) was more than the critical value of t at 1 percent significance level. Results implied that firms with high liquidity tend to use less debt. This indicated that in general, Malaysian firms finance their investments following the financing pattern implied by the pecking order theory. In other words, the more liquid a firm was, the lesser the resort to borrowing. These firms with high liquidity maintain a relatively high amount of current assets and also generate high cash inflows. Consequently, firms use the cash inflows to finance their investments and activities with less reliance on external finance since the firms have sufficient liquid assets. The findings in this study supported the study conducted in Asia Pacific Region (Deesomsak et al., 2004); Saudi Arabia (Al-Ajmi et. al., 2009); Pakistan (Afza and Hussain, 2011) and Palestine (Mouamer, 2011). Additionally, Myers and Rajan (1998) stated that agency costs of liquidity were high and hence external creditors tend to limit the amount of debt financing accessible by the firm. Furthermore, managers of high liquefied firms tend to manipulate the liquid assets in favor of shareholders instead of debt holders will increase the agency costs of debt. Therefore, the relationship between liquidity and leverage was significantly negative.

Firm size was found to have positively significant relationship with leverage. It can be explained that as one unit of firm size increase, there will be an increase of 0.055 unit of leverage. The estimated t- value was 2.11 (p < 0.05) at 5 percent significance level. Findings showed that larger firms face lower bankruptcy costs and thus these firms tend to attain more debt. This was because large firms usually have sufficient resources or capabilities to overcome financial distress. Also, large firms typically employ external finance so as to finance greater investments for future expansions since internal finance would limit the investments. Besides, larger firms may have advantage of accessing credit markets over smaller firms. This may probably be because larger firms especially if they were more established usually gained more trust by the creditors. Wiwattanakantang (1999) pointed out that it is documented in the financial statements of the firms in the sample that many firms, especially large and well-known firms, obtain loans without providing collaterals. Moreover, larger firms were usually more diversified and were less likely to be susceptible to financial distress. This enhances the debt capacity of the firm. Additionally, this result was in line with the static tradeoff theory. Larger firms were more profitable and high profitable firms require a higher target debt ratio to ensure higher tax savings from debt, lower probability of bankruptcy and higher over-investment. Similar results were also reported and supported by studies done in Thailand (Wiwattanakantang, 1999), Asia Pacific region (Deesomsak et al., 2004), Ghana (Amidu, 2007), and Jordan (Al-Najjar and Taylor, 2008).

5. Conclusion
This study had been carried out with the purpose of examining the factors influencing the capital structure decisions in Malaysian firms. The factors included in this study were profitability, tangibility, liquidity and firm size. The relationships between the factors and leverage of firms were tested. In order to achieve the aim of this study, the financial data, which comprised of 69 listed firms out of the FTSE Bursa Malaysia Top 100 Index companies were analyzed covering total sample period of five years from 2007 to 2011. The FTSE Bursa Malaysia Top 100 Index covers around 81 percent of the full market capitalization of the FTSE Bursa Malaysia Emas Index. Thus, this study is significant to represent the Malaysian firms from all sectors except the banking and finance sector, which had been excluded due to the special rules regarding financing. The findings in this study showed that profitability, tangibility, liquidity and firm size were significant and important to determine the capital structure of Malaysian firms. Additionally, profitability
had the highest coefficient value implied that profitability was the most influential factor on leverage. The second most influential factor was tangibility followed by liquidity and finally firm size. These findings can help the managers make a better capital structure decision. Financial managers will be able to determine the best combination of debt and equity that minimizes the cost of capital while maximizing the stock price of the firm.
REFERENCES


