THE RELATIONSHIP BETWEEN CORPORATE GOVERNANCE AND FIRM'S CAPITAL STRUCTURE: MALAYSIAN EVIDENCE

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Dissertation Submitted to

Othman Yeop Abdullah Graduates School of Business

Universiti Utara Malaysia

In Partial Fulfillment of the Requirement for the Degree of Master of Science (Finance)

DECLARATION

I hereby declare that this project paper is based on my original work except for the citations and quotations that are used in this study. All of them have been duly acknowledged. I also declare that this project paper has not previously been submitted to any Master's program in Universiti Utara Malaysia and any other institutions.

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ABSTRACT

This study examines the relationships between corporate governance mechanisms (bankers on board, family-owned company, CEO duality, board size, and board composition), including control variables (firm size, firm age and firm's profitability) with capital structure (debt-equity ratio) of listed companies in Malaysia. This study uses data from 60 largest listed companies, based on their market capitalization, from all sectors in Malaysia except financial institution and insurance companies. The time period covered is from 2000 to 2004, that is, after the announcement of the Malaysian Code of Corporate Governance in 2000. This study finds positive relationships between capital structure and bankers on board, family-owned company, board composition, and firm size. The relationships on family-owned company and firm size are significant, with both have strongly influencing the firms' capital structure. Profitability has a negative relationship. Board size and firm age both have negative, but significant relationships with the firms' capital structure. Generally, the existing literature on the relationships between corporate governance and capital structure has supported the findings of this study.

ACKNOWLEDGEMENT

بسم اللة الرحمن الرحيم

In the name of Allah, the Most Gracious and the Most Merciful

Alhamdulillah. All praise goes to Allah SWT for His kindness, mercy and blessing which has guided me to face all the trials and tribulations to complete this thesis

First and foremost, I would like to express my sincere gratitude and appreciation to my supportive, charismatic, and committed supervisor Associate Professor Norafifah Binti Ahmad, for her constructive comments, encouragement and suggestions. Without her patience and guidance, I might not be able to complete this thesis.

Not to forget, to all my lecturers at Universiti Utara Malaysia who had taught me a lot, thank you very much. To all my classmates, especially Ahmad Harith Ashrofie, Taufiq, Izzatul Amal, Hazwani, Ahmed Hadi, Syed Fairul, Hisham, Anton Eise De Vries, Noraini, Maizatul, Izni and Zaza who had helped me a lot when I was in trouble and down. Thank you for all your support.

Finally, I also would like to express my dedication to my parents, Mr. Anuar bin Md. Zain and Mrs Zaiton Binti Ariffin, and all my family members, for their full moral support and encouragement for me to finish my study. I love everyone of you.

May Allah bless.

Sincerely,

Muhammad Ashraf Bin Anuar.

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BACKGROUND OF THE STUDY

1.1 Introduction

Capital structure is how a corporation finances its assets with a mix of short-term debt, long-term debt, equity, or a mix of securities. In other words, it is how a firm develops a strategy in financing its growth and operation using different sources of financing.

Researchers have placed great concern on capital structure as one of the most important issues in corporate finance (see for example, Hasan & Butt (2009); Huang & Song (2006) and Saad (2010)). This concern arises due to the fact that the mix of financing sources, cost and availability of capital affects the decision making for the companies (Omet & Mashharawe, 2002). While considering investment strategy in the company, a basic understanding about the capital structure is necessary, particularly its level of gearing and a originating point to arrive at a conclusion.

There are a number of theories that have been forwarded to clarify the variation in capital structure for companies. Most of the theories argue that companies choose capital structure because they can verify better the costs and benefits pertaining to financial and equity financing of company, starting with capital structure irrelevance hypothesis as explained by Modigliani and Miller (1958)**,** followed by financial

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