THE SIMULTANEITY OF FINANCING AND INVESTMENT DECISIONS IN THE PRESENCE OF CORPORATE GOVERNANCE FACTORS

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THE SIMULTANEITY OF FINANCING AND INVESTMENT DECISIONS IN THE PRESENCE OF CORPORATE GOVERNANCE FACTORS

By

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This study investigates the interdependence between financing and investment decisions in the presence of corporate governance factors of three hundred non-financial companies listed on the Main Market of Bursa Malaysia. The sample is chosen randomly over a five-year period from 2007 to 2011. Using a panel data methodology, the regression models are derived based on the simultaneous equation modeling. Six factors of corporate governance mechanisms are identified: family ownership, government ownership, state ownership, managerial ownership, board size and board composition. This is among the earliest studies in Malaysia to consider simultaneity of financing and investment decisions by adopting 2SLS estimation technique. The major contributions of this study are: first, financing and investment decisions must be determined simultaneously. The results show that both investment and financing have positive impacts on each other. This positive effect is significantly stronger for firms with high-growth opportunities than those with low-growth opportunities. Second, government link investment companies (GLICs) affect leverage positively but affect investment opportunities negatively. For that reason, the government should monitor GLICs’ investments as firms controlled by GLICs have lower investment opportunities. This is especially true for low-growth firms. In contrast to GLICs, state ownership leads to higher investment opportunities especially for low growth firms. Third, managers of high-growth firms are doing their job more effectively compared to those of low growth-firms in making investment decision. Fourth, independent directors do not play a significant role regarding investment policy especially for low growth firms. Finally, since profitability is significant for all financing models, the finding of this study supports pecking order theory.

**Keywords:** financing, investment, corporate governance, 2SLS
ABSTRAK


Kata Kunci: pembiayaan, pelaburan, tadbir urus korporat, 2SLS
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<td>Investment Opportunity Set</td>
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<td>GDP</td>
<td>Growth Domestic Product</td>
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<td>NPV</td>
<td>Net Present Value</td>
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<td>OLS</td>
<td>Ordinary Least Square</td>
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<td>2SLS</td>
<td>Two Stage Least Square</td>
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<td>GMM</td>
<td>Generalized Method of Moments</td>
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<td>Government Linked-Investment Companies</td>
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<td>MAS Berhad</td>
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<td>EBIT</td>
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CHAPTER ONE
INTRODUCTION

1.0 Introduction

This chapter starts with section 1.1 which provides the background of the study. Section 1.2 presents problem statement. Section 1.3 discusses research questions. Research objectives are discussed in section 1.4. In section 1.5, the scope of the study is examined. The significance and contribution of the study are explained in section 1.6. This chapter ends with the structure of the thesis in section 1.7.

1.1 Background of the Study

The importance of corporate firms in generating a country’s higher productivity and better economic growth is undeniable in today’s globalization era. To play the role, the firms’ managers must ensure that their corporate funds and resources are utilized efficiently so that they can be transformed into productive activities. Since managers must always adopt actions that work in favor of the interest of the shareholders, they must only invest in projects that promote greater productivity and efficiency. Such projects usually need considerable investments in current technologies, building development and promotion of products. It is the responsibility of the firm’s corporate finance department to manage these financing and investment decisions.

There are many alternatives that can be employed by firms to fund or finance their investments. One of them is debt. Together with equity and retained earnings, debt is definitely among the top capital structure elements of the firm. Financial leverage is the common term used to describe the debt level employed to pay for firm assets and
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