EUROPEAN ACADEMIC RESEARCH
Vol. VI, Issue 9/ December 2018

Impact Factor: 3.4546 (UIF)
DRJI Value: 5.9 (B+)

ISSN 2286-4822
www.euacademic.org

Foreign Ownership, Governance Practices and Gearing Level: Evidence from Pakistan Stock Exchange

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Abstract

The aim of this study is to find out the impact of ownership structure and corporate governance on capital structure of the 56 companies of PSE 100 index. It explores the impact of foreign ownership and corporate governance factors on capital structure. In this research secondary data is used by annual reports of the companies of Pakistan. In this study, foreign ownership is negatively related to debt ratio and statistically significant. This finding suggests that higher the foreign ownership in the firm lower will be the debt ratio of the firm. Previous studies like Gedajlovic et al.(2005) supported previous studies that there exist negative relationship between foreign ownership and capital structure. This finding suggests

that large board size favors higher debt ratio Large companies have large board size and such companies with giant assets take debt on favorable terms. Large board size results in low debt cost because creditors think that the firm is under strict supervision of the diversified board. Coles et al. (2008) reports a positive relationship between board size and capital structure in American context. They provide a possible explanation for this is that firm with high gearing ratio may have larger advising requirements then firms with low gearing levels. (2004) also found positive relationship between board size and debt ratio, he argues that firm with higher boards have easy access to debt at favorable terms. This finding suggests that CEO duality leads to firm's lower debt usage. Higher the board independence higher the leverage of the firm. Firm size is positively related to the leverage of the firm and has a significant positive impact on leverage. This means that larger the firm size higher will be the debt.

Key words: Foreign Ownership, Board Size, Board Independence, CEO Duality Capital Structure

1. INTRODUCTION

Capital structure of a firm broadly consists of debt and equity. Capital structure is a portion of a company's balance sheet which consists of debt and owner's equity. The issuance of long term debt or short term debt depends on firm's financial strategy. Modigliani and Miller (1958) first introduce the capital structure theory. Many researchers have done work and extended the capital structure theory but a few have done work on the relationship between capital structure and corporate governance. Good corporate governance practices help to create trust between investors, lenders and the firm. Corporate governance is essential for the firm to make continuous growth. Thus for the growth of the corporate sectors of any country corporate governance practices are necessary to be

implemented. The constituents of corporate governance involve board of directors who hire fire and take decisions regarding managers remuneration. The concept of corporate governance includes disclosing information to shareholders, board of directors, senior management remunerations, reducing conflict of interest between managers and shareholders and provides supervisory structure to the firm. High quality corporate governance motivates the managers to increase the shareholders wealth and it also reduces agency costs. The alternative of agency cost is now replaced by modern corporate governance practices which supervise the management. This system of corporate governance consists of shareholders, managers and a board of directors. Corporate governance practices are the building blocks of corporate strategy like outside financing. Firms with weak or no corporate governance structure face high agency problems and managers put their motives or goals ahead than the corporate goals leading to deteriorating situation. The Cadbury Report (1992) defines corporate governance as the ways through which companies are directed and controlled. "Corporate governance deals with the rights and responsibilities of a company's management, its board, shareholders and various stakeholders" (OECD)."Corporate governance rules are made to regulate the relationships among different parties of the companies like managers and shareholders, employees and creditors. Berl and Means were the first who introduce the corporate governance topics. Corporate governance includes techniques to resolve two types of conflicts. In 1998 finally UK issued a Combined Code of Corporate Governance which was enforced on all the listed companies in the country. In Pakistan in comparison with other developed countries, there still exists weak external and internal corporate governance structure. There exist some international bodies which provide guidance on corporate

governance like The WB, The Global Corporate Governance Forum, IMF, International Corporate Governance Network etc.

1.1 Corporate Governance Practices (SECP, 2012 Pakistan)

In Pakistan as compared to developed nations, still there exist fragile internal and external corporate governance practices. Pakistani companies are rapidly accepting the corporate governance culture in their organizations. The government is showing its keen interest in corporate governance practices. SECP took initial step for establishing corporate governance codes in Pakistan and issued corporate governance codes in March 28, 2002. Many institutions are working in Pakistan to arise the importance of corporate governance in a company like some are ICAP, Pakistan Institute of Corporate Governance (PICG). State Bank of Pakistan is working on creating and implementing good corporate governance structure. Corporate governance and ownership structure is an emerging concept in finance school of thought. Various researchers have conducted their research study on corporate governance practices by using different variables and their relation with various dependent variables like corporate performance, dividend policy, capital structure, firm value. Corporate governance is an evolving area of research. The impact of foreign ownership and corporate governance on capital structure has not been fully explored. Earlier studies were on the relationships between capital structure and ownership structure by (Arslan and Zaman, 2014) and Masood (2014) (Ahmed and Wang,2012) to check the effect of corporate governance on the capital structure .No research has been found to investigate the impact of both foreign ownership and corporate governance on capital structure in Pakistan.

2. Literature Review

After pivotal contribution in literature of Modigliani & Miller (1958) more than few theories of capital structure have been introduced, pecking order theory trade off theory and agency theory stand as key philosophies of firm's financial choice of capital structure both in developing and developed economies and there were lot of research studies conducted to explain the choice of capital structure of the firms, by using pecking order theory and trade off theory and have consistent results (Lingling Zhang, 2013). This section will review literature pertinent to the study; precisely it will focus on the theories and empirical studies conducted by many researchers. So, this study will focus on the agency theory to investigate probable organizational clashes and their effect on the firm's choice of capital structure.

2.1 The Agency Cost Theory:

The agency relationship can be summarized as "a contract in which one person hires another person to work and take decisions on his behalf by delegating some decision making powers". Shareholders are the sole owners of the firm and management is responsible to run the company so that shareholder's interests are fulfilled. Thus the duty of the management is to maximize the shareholder's wealth. A conflict of interest may arise between the parties in the company when they take financial decisions, it can be between managers and shareholders and between shareholders and creditors (Jensen 1986: Jensen and Meckling 1976). As in a company management and owners are separated therefore there always exists a chance of that managers may put their goals ahead than the corporate goals. It means than there is a probability that managers want to take excess free cash flow for their personal use rather than involve in activities which lead to maximize the shareholders wealth. Therefore shareholders

always consider that management is not involved in such projects which are unprofitable having negative NPV. The free cash flow must be distributed among shareholders through dividend or in case of higher debt ratio they invest in such projects which have positive NPV value so that contractual interest payments are met periodically. Shareholders bear some costs to mitigate this issue called agency costs. If it is required that higher the need mangers must be controlled higher will be the agency cost. These costs are discussed by free cash flow hypothesis. Thus this cost may determine capital structure (Jensen 1986). Increased debt position of the company forces the managers to use excess free cash flow to pay the interest and repayments. Thus debt may help the company to mitigate the agency costs (free cash flow). However there exists a chance that probably the company might fail to repay interests and loan thus increasing bankruptcy risk. But this bankruptcy risk may make the managers to work harder and make correct and valuable investments thus decreasing bankruptcy risk (Grossman and Hart 1980). Another agency cost is debt financing cost between debt holders and shareholders (Jensen and Meckling 1976). First, the shareholders may make high risk investments to make high returns but damaging debt holder's interests. Thus shareholders may make risky investments even they are decreasing its value (Harris and Raviv 1991). Secondly, when firm has high amount of debt and investing in high value projects will make it repaying the debt. In this case the shareholders will not make such investments (Myers 1977). Similarly the large shareholders consider their interests more important and beneficial over the minority shareholders. Large shareholders may make wealth by expropriating minority shareholders (Shleifer and Vishny 1997). Firm value decreases in such a situation.

2.2 Capital Structure

Margaritis and Psillaki (2010) defined that capital structure is the mixture of debt and equity that is conserved by a fir to finance its operations. They argued that is important for a firm to maintain optima capital structures that ensure the maximization of the firm's value. By choosing the optima capital structure it reduces the firm's cost of capital and in turn maximizes the value of the firm. Weston and Brigham (1992) also described that optimal capital is one that maximize the market value of the outstanding shares of a firm. It is argued that there is a hierarchy of preferences in order to financing decisions, that is the pecking order theory which suggests that the firms financing needs will be fulfilled by the internal sources like un distributed earnings and then they will use the debt in case of additional funds needed (Myers,1984). When a firm uses the portion of debt in their capital structure it leads to the agency cost. Agency cost theory presented by Jensen and Meckling (1976) and they articulated that a firm may fail to maximize its value due to agency conflicts that are the preferences differences and the split up of the ownership and management styles. Conflicts between owners and creditors may arise due to the preferences differences and different assertions on the firm. Myers (2001) presented a hypothesis that firms use a higher level of debt in their capital structure for gaining the maximum benefit of tax and in this way firms maximize their profitability level. As by using more debt in their capital structure increases the possibility of deduction of interest from company tax as this finding is aligned with (Modigiliani and Miller, 1963).

Demsetz and Vilalonga (2001) measure the leverage and Tobin's Q by taking as endogenous variables which means that the two way causal relationship between the variables. They concluded that firm's performance is affected by the capital structure which in turn affects the capital structure. O'Connell

and Cramer (2010) described the relationship between the performance of the firm and leverage. Findings of the study revealed that there is significant and positive relationship between firm value and leverage. Moreover, findings of their study specified that there is positive impact of high debt level on the performance of the firm. The high level of debt improves the market performance of the firm. Saeedi and Mahmoodi (2011) conducted a study in which they examine the relationship between capital structure and performance of the firm. The results of the study reconnoitered that capital structure has positive association with Tobin's Q. Similarly Salim and Yadav (2012) also studied the relationship between capital structure and the firm's performance and they concluded that Tobin's Q was negatively significant and correlated to capital structure. According to the study of Bender (2013) revealed that life stage of a firm may influence the capital structure. As the Firm's situations may change the financing needs. They also provide the evidence that business risk of a firm moderates during the life stages of the firm whereas financial risk increases.

2.3 Foreign Ownership and Capital Structure

Foreign ownership is defined as "the control of a resource or a business in a country by individuals or companies who are not that country citizens or headquartered in that country". Foreign ownership occurred in a country when a multinational company or foreign government directly invests in that company. If foreign company holds 50% or more shares in a company it becomes holding company and acquired company is called subsidiary company. Godfred A. Bokpin et al (2009) concludes that foreign ownership is positively related to capital structure. The performance of the firm is increased by foreign ownership thus it enhances corporate governance practices in the firm. Present study includes the definition of foreign ownership as as

"the percentage ownership of foreign investors, individuals or companies". On the other hand some studies also find a negative relationship between foreign ownership and capital structure like Kocenda and Svejnar, (2002) Li et al. (2009) Lee and Kwok(1988) Mieno(2009) and Gurunlu and Gusrsoy(2010) finds that firms with high foreign investment in their equity have low gearing level because these companies mostly have high level of retained earnings to finance their projects internally. Previous studies like Gedajlovic et al.(2005) supported previous studies that there exist negative relationship between foreign ownership and capital structure. Tamimi (2011) conducted a study to find out the impact of foreign ownership on capital structure, the study find a negative relationship between foreign ownership and capital structure. Investor's interest in a firm can be determined by the performance of the firm and corporate governance can play a role of moderation and protection. With the role moderation corporate governance can mediate the activities of the managers but on the other hand with the role of protection it can protect the interests of the stakeholders and firm.

Rocca (2007) emphasized that corporate governance plays an important role in determining the capital structure of a firm. She emphasized that corporate governance played the role of mediation between the level of leverage and firm value. She also provided the evidence that capital structure motivated the effective corporate governance that in turn used the financing to minimize the level of information asymmetry problem. Likewise, it was also concluded that corporate governance has a mediating effect between the capital structure and value of the firm. Javeed et al. (2014) discussed the impact of corporate governance measures on the value of the firms and then they also studied the relationship between the capital structure and firm value. They used 775 observations of 155 non-financial firms and listed at Karachi stock exchange

covering the period 2008-2012. Fixed effects regression model was used for the analysis of panel data. The results of the study showed that there is a significant and positive impact of capital structure on the value of the firm whereas in corporate governance measures board independence and ownership concentration significantly and positively influence the firm value. Ganjyu and Abioun (2012) found that corporate governance measures such as board size, board skills and CEO duality have a momentous impact in the determination of debt to equity ratio in the food and beverage industry of Nigeria. Moreover, they also concluded that larger size of boards and higher level of profitability may dispose the firms to take the more risks by availing the option of external financing for the growth of the business and misuse of investment opportunities. Ukaebgu et al (2014) examined the relationship between corporate governance and capital structure and also checked the impact of this association on the firm value. The sample used in this study was non- financial Nigerian firm's panel data. The results of the study disclosed the inverse relationship between capital structure and firm's performance as the capital structure of most Nigerian firms was subject to the short term leverage. Moreover, the results revealed that the positive connection between the firm's performance and leverage, board meetings and board size but it was inversely related to the board composition.

2.4 Board Size and Capital Structure

In Pakistan, the largest board size is 19 and minimum board size 7. Company Board plays a pivotal role in the better governance and proper functioning of the company. They are held responsible for the firm operations. They play their part in deciding financial mix of the company. Pfeffer and Salancick (1978) conclude that size of board has significant effect on capital pattern of the firm. Berger (1997) concludes that large

board size tends to low gearing levels. According to him large board size keeps the managers to maintain low debt level and increasing the performance of the firm. Abor and Biekpe (2007) find that size of board and leverage are negatively related and low gearing level is found in SMEs having larger board size. On the contrary, Wen (2002) concludes that size of board is positively related to capital structure. He says that high gearing level due to the large board size increases the firm's value. He also mentions that due to large board size, its member take no early consensus on any decision which may affect the governance and ultimately results in high debt level. Large board size results in low debt cost because creditors think that the firm is under strict supervision of the diversified board. In this study it is defined as "the total number of members of the board as disclosed in annual report". For the success of an organization there is always the need of an effective board as this is the highest body in a company that is accountable for decision making that will enhance the growth of the firm ultimately. In the study of Mak and Kusnadi (2005) negative relationship was found between the size of the board and value of the firm. Cheng (2008) examined a study in which they provide the relationship between the performance of the firm and the size of the board. They provide the evidence of negative relationship between these variables. Moreover, they concluded that there is less changeability in the performance of the firms as the size of the board enlarges and suggested that intention of less change in the performance of a firm is that larger size board's decisions are less inspiring. In another stud that is conducted by O'Connell and Cramer (2010) in which the association between size and corporate performance was explored by taking the sample of smaller firms. They provided the evidence of inverse relationship between board size and performance of the firms as board size has less impact on the corporate performance.

Uchida (2011) found the relationship between corporate downsized board and the shareholders' value. They used the data of Japanese companies and concluded that there are no improvements in the performance of the companies by downsized boards. Ramos and Olalla (2011) reported a comparative study in which they checked the impact of board size in founder led family and non-founder led family businesses. They concluded that size of the board has a positive impact on the non-founder led family business performance. The evidence of negative impact of board size on the founder led family business performance was found in their study. Adams and Mehran (2012) examined the impact of bank board size on the performance of the companies. They used the sample of large banking holding companies and argued that board size is significantly associated with the performance of the banking companies. Likewise, they further suggested that for the governance of banking companies there should be the distinctive features of governance procedures. Kumar and Singh (2013) provided the evidence of significant and opposite relationship between the sizes of the board firm performance by using the sample of Indian firms.Rajangan et al (2014) checked the impacts of board size and ownership structure on the profitability and gearing level of the firm by considering the sample of Malaysian companies. They concluded that independent directors and executive directors have an influence on the gearing level of the firm whereas the non-independent and non-executive directors have no relation with the performance of the firms. Coles et al. (2008) reports a positive relationship between board size and capital structure in American context. They provide a possible explanation for this is that firm with high gearing ratio may have larger advising requirements then firms with low gearing levels. Anderson et al. (2004) also found positive relationship between board size and debt ratio, he argues that firm with higher boards have

easy access to debt at favorable terms. According to agency theory jansen(1986) and Wen et al. (2002) reports positive relationship between board size gearing ratio. They argues that lager boards are more entrenched due to effective monitoring pursue higher gearing level to boost up the firm value.

2.5 CEO Duality and Capital Structure

A modern corporate governance variables CEO duality also called chair duality. It means that CEO is also the chairman of the board of the company. But it may create an agency problem. This type of situation has direct effect on financial mix of the firm. Fama and Jensen (1983) conclude that decision control function is separated from decision management function. Decision management function includes initiating and executing new proposals and decision control function includes approving and monitoring such proposals. The absence of this separation leads to agency costs. Fosberg (2004) found that optimal capital structure is present in the firms in which there is separation of chairman and CEO posts thus showing that such firms have higher leverage. But in Fosberg (2004) study statistics show that this relation is insignificant. Abor and Biekpe (2007) found positive relation between CEO duality and leverage. Nazir et al (2012) presented a study in which they explored the impact of CEO duality on the capital structure by selecting the 269 non-financial firms listed at the Karachi stock exchange for the period of 2004-2009. They eliminated the effect of default, new and 5% trim data. Generalized regression model was used for the analysis of the data and they concluded that CEO duality has positive and significant relationship with the leverage of the firm but have the indirect relationship with the tangibility. CEO duality has been one of the most debated topics in corporate governance. The believers of agency theory entreat about the negative impact of the CEO duality (Jensen & Meckling, 1976; Fama& Jensen, 1983) whereas on the other

hand the advocates of the stewardship theory argued that CEO duality has positive influences on capital structure (1997; Bhagat& Black, 2001).Lam and Lee (2008) examined the relationship between CEO duality and firm performance. The results of the study argue that relationship between CEO duality and firm performance is conditional that CEO duality has less impact on the value of the firm in case of family control businesses and likewise duality position was found good for non- family firms. Fosberg (2004) conducted a study to investigate the impact of corporate governance and capital structure; he found that CEO duality is positively related to gearing level. The author provides the explanation for this positive relationship is leadership duality lessens the problem of separation of ownership and control and therefore has high accessibility to the debt on favorable terms. Like the Fosberg(2004), Faleye (2004) also reports the positive relationship between CEO duality and capital structure, he provide the explanation for this relationship that Duality in leadership may lessens the problem of information asymmetry in turn this leads to higher access to external finance. Positive relationship between dual leadership and capital structure also reported by the Abor(2007).

2.6 Board independence and Capital structure

An outside director is a member of the board of the company but does not participate in the executive management of the company. It is also called outside director and abbreviated as NED, NXD, non-exec, external directors, independent directors, director at large. External directors challenge the performance of management, executive directors and take a strong stand to protect the interest of the firm and its stakeholders. They are equally liable as the executive directors of the firm. The presence of the independent or outside directors on the board shows to the market that the company is under strict

supervision and investors think that company is working efficiently. The creditors consider it credit worthy thus it makes easy for the firm to take debt from outsiders. Outside directors are the key part of the corporate governance. According to Pfeffer and Salancick (1978) the presence of external directors on the board is much appreciated by the outsiders who have made their investments in the company. This makes the firm's images better in the eye of investors. Their study shows results that higher board independence increase leverage. Jensen (1986) and Berger et al (1997) found that high leverage is found in the firms which have high representation of non-executive directors and firms with low number of external directors have low debt level. According to Abor and Biekpe (2007) chair duality and composition of board is positively related to capital structure. However, Wen (2002) concludes that board independence is negatively related to gearing level. The outside directors have better control on managers thus forcing them low debt level. In this study board independence is defined as "the number of non-executive directors by the total number of directors on the board". It is expressed in percentage. There is desirability of independent directors on board because they have to see the actions of the management and taking the corrective governance actions. Erickson et al. (2005) determined the composition of board and its effect on the value of the firm by using the data from Canadian companies. They found the negative connection between the board independence and firm value. They argued that poorly performing firms encourage the presence of outside directors on the board in successive periods. Lefort and Urzua (2008) reported a study in which they worked on the independence of board, value of the firm and ownership concentration by using the data from Chile. They provided the evidence that increase in the level of independence of a board has an influence on the performance of the firm. Duchin et al. (2010) instituted that increased independence of directors

neither harm not improve the performance. Motavassel et al (2013) also found the evidence of insignificant relationship between the outside directors and firm value. Ahmed and Wang (2010) investigated the relationship between corporate governance and capital structure. The study used the data of non- financial firms listed at PSE for the period of 2004-2008.Corporate governance measures like board size, outside directors are found to be having positive relationship with capital structure. The study supported that corporate manager by establishing the optimal capital structure and by institutional support can enforce the effective corporate governance mechanism.

3. Data and Methodology

The aim of this study is to find out the impact of ownership structure and corporate governance on capital structure of the 56 companies of PSE 100 index. It explores the impact of foreign ownership and corporate governance factors on capital structure. In this research secondary data is used by annual reports of the companies of Pakistan. Both domestic and international articles are studied to make the basis of this research.

3.1 Data and Sample

In this study, it includes local firms of Pakistan listed in Karachi Stock Market (PSE) which is the biggest stock market of the country called as PSE 100 index. This research covers the period from 2011 to 2014 which involves most recently published information by the companies. This period of four years was selected because it is latest and this period is showing the developments in growing capital market of Pakistan. During this period new concept in modern firms called as corporate governance is being appreciated by the

companies of Pakistan. The selected period and firms are chosen unbiased. This study focuses on the PSE 100 index companies of Pakistan and financial reports of all the companies have been downloaded by their respective websites. All these firms are non-financial firms because the capital structure of non-financial firms is different from the capital structure of the financial firms and by combing the both the results do not show the real phenomena. The reason for selecting the PSE 100 index companies is that these companies are the best performer of Pakistan and therefore examination of ownership pattern and corporate governance practices in these companies is necessary so that other companies set these companies as their benchmark such researches might help the government in policy making. In order to conduct this research, the sample size 56 companies and these companies are randomly selected and those are chosen whose four year annual reports from 2011-2014 are available and the information regarding the variables of this study also presented in these reports.

3.2 Sample and Sample Size

- PSE 100 index consist of 100 companies
- Out of 100 companies 24 are related to financial sector, 76 companies are related to none-financial sector
- This study includes the four year data of 56 firms out of 76 none financial firms, 20 firms are excluded due to the unavailability of data.
- So out of 304 observations of 76 firms this study includes 224 observations of 56 firms

3.4 Data

Secondary data is used in this study that is collected from the annual reports of the respected firms. Annual reports were

collected from different sources like the official website of the firm and from the PSE official website.

3.5 Data Analysis techniques

After collecting and arranging the data E-views7 is used to analyze the data. Pooled OLS is used to investigate the impact of foreign ownership and corporate governance on capital structure of the PSE listed firms.

3.6 Variables

3.6.1 Dependent Variable

Capital structure is used as dependent variable. Various researchers have used different definitions of capital structure in their work like some are: total debt divided by total assets (Eduardo J. Menendez-Alonso and Silvia Gomez-Anson, 2003), debt to equity ratio (Arshad Hasan and Safdar Ali Butt, 2009), long term debt divided by total assets (Zou and Xiao, 2006). This study quantifies capital structure as total debt to total assets. Total debt includes all the liabilities like short term debt, long term debt and any other kind of debt like loan taken from relatives, friends etc. Thus in liabilities and owner's equity part of the balance sheet all liabilities excluding owner's equity are taken as total debt. The definition of capital structure used in this study is used as leverage in (Eduardo J. Menendez-Alonso and Silvia Gomez-Anson, 2003),(Wellalage and Locke, 2014) and (Masood, 2014) studies. Foreign ownership is defined as "the percentage share held by foreign investors, individuals or companies". In this study CEO duality is a dummy variable .1 is taken if CEO also chairs the board otherwise it is taken as 0. This definition is used in (Hasan and Butt, 2009) Board independence is defined as "the number of non-executive directors on the board". This definition is used in (Ahmad Ahmadpour et al, 2012). The main focus of this study

tests the effect of foreign ownership and governance on capital structure of firms. But still there are some variables that influence aforesaid relationship and possibly would contaminate the results of the study so these (above mentioned) variables are required to fix as control variables in the analysis, So that they cannot pollute the results. Control variables used in this study are firm size, profitability, assets tangibility and liquidity.

3.7 Model Specification

$$CS=\alpha+\beta_1 FOS+\beta_B BSIZE + \beta 3BIND+ \beta 4\ CEOD+ K+\mu$$

α= Represented Constant
ß= Beta Coefficients
FOS=Foreign Ownership
BIND=Board Independence
BSIZE= Board Size
CEOD=CEO Duality
K=Control Variable
μ= Error Term

4. Results and Discussion

Table No. 1

	Simple OLS Model 1		**OLS Heteroskedastic Model 2**		**ML - ARCH (Marquardt) - Normal distribution Model 3**	
Variable	**Coefficients (Prob)**	**t-Statistics**	**Coefficients (Prob)**	**z-Statistics**	**Coefficients (Prob)**	**z-Statistics**
Foreign Ownership	-0.001407 (**0.0089*****)	-2.640328	-0.000520 (**0.0003*****)	-3.657948	-0.002730 (**0.0000*****)	-0.751851
Board Independence	0.015479 (0.1088)	1.610297	0.003807 (0.1390)	1.485091	-0.012339 (0.1244)	8.504387
Board Size	0.042806 (**0.0012*****)	3.273212	0.000813 (0.8158)	0.233223	0.037534 (**0.0003*****)	1.536414
CEO Duality	-0.037657 (0.3810)	-0.877923	-0.018849 (0.1009)	-1.647704	-0.053213 (**0.1018***)	-3.607366
Assets Tangibility	0.001687 (**0.0019****)	3.144262	4.06E-06 (0.9774)	0.028332	0.000947 (**0.0074*****)	1.636029
Profitability	-0.002469 (0.0622)	-1.874590	-0.001713 (0.0000***)	-4.876956	-0.004205 (**0.0000*****)	-2.677511
Liquidity	-0.004290 (**0.0016*****)	-3.201603	-9.90E-05 (0.7821)	-0.276908	-0.007363 (**0.0000*****)	-5.459071
Firm Size	0.042822 (**0.0007*****)	3.446912	0.002665 (0.4220)	0.804469	0.050583 (**0.0000*****)	5.986673
R^2	*0.241321*		*0.175681*		*0.184040*	
ADJ. R^²	*0.213092*		*0.145009*		*0.153678*	
N	**56**		**56**		**56**	

Note:*** denotes the level of significance of 1%,** denotes 5% level of significance and * denotes 10% level of Significance

Breusch-Pagan-Godfrey test is utilized for controlling heteroskedasticity. Probabilities show that there exist heteroskedasticity in data. So to control the problem of heteroskedasticity ML - ARCH (Marquardt) - Normal distribution test is used. This following table showing the results of ML - ARCH (Marquardt) - Normal distribution test.

4.2 Results & Discussion after Controlling Heteroskedasticity

In this study, foreign ownership is negatively related to debt ratio and statistically significant. This finding suggests that higher the foreign ownership in the firm lower will be the debt ratio of the firm. Thus foreign owners favor less debt and this is consistent with the pecking order theory in which the firm must finance its projects by internal sources. On the other hand some studies also find a negative relationship between foreign ownership and capital structure like kocenda&svejnar, (2002) Li et al. (2009) Lee and kwok(1988) Mieno(2009) and Gurunlu& Guernsey(2010) finds that firms with high foreign investment in their equity have low gearing level because these companies mostly have high level of retained earnings to finance their projects internally. Previous studies like Gedajlovic et al.(2005) supported previous studies that there exist negative relationship between foreign ownership and capital structure. Tamimi (2011) conducted a study to find out the impact of foreign ownership on capital structure, the study find a negative relationship between foreign ownership and capital structure.

In this study, Board size is positively related to debt ratio and statistically significant. This finding suggests that large board size favors higher debt ratio Large companies have large board size and such companies with giant assets take debt on favorable terms. Wen (2002) concludes that size of board is positively related to capital structure. He says that high

gearing level due to the large board size increases the firm's value. He also mentions that due to large board size, its member take no early consensus on any decision which may affect the governance and ultimately results in high debt level. Large board size results in low debt cost because creditors think that the firm is under strict supervision of the diversified board. Coles et al. (2008) reports a positive relationship between board size and capital structure in American context. Anderson et al. (2004) also found positive relationship between board size and debt ratio, he argues that firm with higher boards have easy access to debt at favorable terms. According to agency theory Jansen(1986) and Wen et al. (2002) reports positive relationship between board size gearing ratio. They argues that lager boards are more entrenched due to effective monitoring pursue higher gearing level to boost up the firm value.

In this study, CEO duality is negatively related to debt ratio and statistically significant. This finding suggests that CEO duality leads to firm's lower debt usage. If CEO is also the chairman of the board lower will be the debt ratio of the firm. CEO duality in fact reduces separation of ownership and information asymmetry in the firm. According to Abor and Biekpe (2007) chair duality and composition of board is positively related to capital structure. Fosberg (2004) conducted a study to investigate the impact of corporate governance and capital structure; he found that CEO duality is positively related to gearing level. The author provides the explanation for this positive relationship is leadership duality lessens the problem of separation of ownership and control and therefore has high accessibility to the debt on favorable terms. Like the Fosberg(2004), Faleye (2004) also reports the positive relationship between CEO duality and capital structure, he provide the explanation for this relationship that Duality in leadership may lessens the problem of information asymmetry in turn this leads to higher access to external finance. A

positive relationship between dual leadership and capital structure also reported by the Abor(2007). A possible explanation for relation in the context of Pakistan is that mostly firms are owned by families there also exist duality in leadership so they choose more debt financing over equity financing because they want to dilute their ownership.

In this study, Board independence is positive related to debt ratio and statistically significant. This finding suggests that if board of the firm consists more number of outside and non-executive directors then higher will be the debt ratio or leverage of the firm. Higher the board independence higher the leverage of the firm. The creditors consider it credit worthy thus it makes easy for the firm to take debt from outsiders. Outside directors are the key part of the corporate governance. According to Pfeffer and Salancick (1978) the presence of external directors on the board is much appreciated by the outsiders who have made their investments in the company. This makes the firm's images better in the eye of investors. Their study shows results that higher board independence increase leverage. Jensen (1986) and Berger et al (1997) found that high leverage is found in the firms which have high representation of non-executive directors and firms with low number of external directors have low debt level. According to Abor and Biekpe (2007) chair duality and composition of board is positively related to capital structure. Firm size is positively related to the leverage of the firm and has a significant positive impact on leverage. This means that larger the firm size higher will be the debt. Titman &Wessels (1988) argued that big firms not consider the bankruptcy cost in deciding the level of leverage as these are just a small percentage of the total value of the firm so larger firms may prefer to use high level of leverage. Friend and Lang (1988), Marsh (1982) also find the positive relationship between firm size and gearing level.

This study finds the profitability is negatively related to the gearing level of the firm. Myers and Majluf (1984) argued that profitable firms have low level of leverage because they prefer to finance their projects by internally generated fund over debt. These findings are in line with the pecking order theory of capital structure. This study finds that Liquidity is negatively related to the leverage level of the firm. According to El-Masry, B Al-Najjar, P Taylor (2008) firms with more liquid assets may use their liquid assets as source of finance to fund future products and projects so that why there exist negative relationship. According to Myers and Rajan (1998) there exist negative relationship between firm liquidity and gearing level. They explained this as the agency costs of liquidity increase outside creditors limit the amount of debt available to company. Firms with high liquidity use low level of external financing (Lingling Zhang, 2013).

5. Conclusion

In this study, foreign ownership is negatively related to debt ratio and statistically significant. This finding suggests that higher the foreign ownership in the firm lower will be the debt ratio of the firm. Previous studies like Gedajlovic et al.(2005) supported previous studies that there exist negative relationship between foreign ownership and capital structure. This finding suggests that large board size favors higher debt ratio Large companies have large board size and such companies with giant assets take debt on favorable terms. Large board size results in low debt cost because creditors think that the firm is under strict supervision of the diversified board. Coles et al. (2008) reports a positive relationship between board size and capital structure in American context. They provide a possible explanation for this is that firm with high gearing ratio may have larger advising requirements then firms with low

gearing levels. (2004) also found positive relationship between board size and debt ratio, he argues that firm with higher boards have easy access to debt at favorable terms. This finding suggests that CEO duality leads to firm's lower debt usage. Higher the board independence higher the leverage of the firm. Firm size is positively related to the leverage of the firm and has a significant positive impact on leverage. This means that larger the firm size higher will be the debt. Friend and Lang (1988), Marsh (1982) also find the positive relationship between firm size and gearing level. According to Myers and Rajan (1998) there exist negative relationship between firm liquidity and gearing level. Firms with high liquidity use less level of external financing (Lingling Zhang, 2013).

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