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Impact of Financing Decision on the Firm value of Listed Manufacturing Companies in Nigeria

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Abstract

This study examined the influence of equity on the firm value of listed manufacturing companies. The study used ex-post facto research design and secondary data for a period of 2014 – 2018. Data obtained from Annual Report and Accounts of sampled six quoted manufacturing companies by the Nigerian Stock Exchange. The study employed Descriptive Statistics and Ordinary Least Square-Linear Regression methods. The results indicated that there is a significant relationship between total equity and firm value of manufacturing companies as confirmed (F -statistics = 5.488, $P < 0.05$). It could be concluded that total equity has positive and statistical significant impact on firm value. The study suggested that firms should time the equity market to determine when equity capital becomes cheaper as compared to debt capital.

1. Background of the Study

Financing decision relates to the raising of finance from various sources depending on the type of source, period of financing, cost of financing and the re-turns. Pandey (2005) cited in Samuel, Ebenezer and Xicang (2012) shared that the capital structure decision of a firm should be examined from the point of its impact on the value of the firm. He further states that if capital structure decision can affect a firm's value, then firms would like to have a capital structure which maximizes their value. The aim of a firm should centre therefore on the maximization of its value through capital structure decisions (Samuel et al, 2012). Alfred (2007) suggested that a firm's capital structure implies the proportion of debt and equity in the total capital structure of the firm. Finance is so vital and serves as an instant cause for companies not commencing or progressing. Capital structure serves as one of the important variables considered by firms when considering financial performance (Ajibola , Wisdom& Qudus, 2018).

Considering a firms capital structure is imperative not just to boost earnings but also its effect on organization's capability to manage competitive environments. The aim of a firm's capital structure may not be focused on wealth maximization but to safeguard management's interest mostly in firms where control is dictated by directors and shares of the corporation carefully held (Dimitris and Psillaki, 2008) as cited in (Ajibola et al, 2018) Consequently, firms should be able to improve their market share, finance operations and grow in the long run to improve value added and profits.

Manufacturing firms listed on the Nigerian Stock Exchange are financed by equity and debt. The positive bias towards equity financing may be due to financial regulations making equity financing more accessible to firms than debt, or firms preferring equity to debt financing as a result of lower cost of capital (Adelegan, 2006). Chowdhury and Chowdhury (2010) viewed that in agency-cost models, financing decisions affect value of firm because they produce behavior that affects profitability. The agency effects of financing decision work through profitability and they can make firms to take better or worse investments and to use assets more or less efficiently. In the pecking order model and asymmetric information problems that arise when issuing debt and equity cause firms to prefer internal financing. External financing is seen as bad news about earnings (Lawal, 2014). Therefore, firm value is equal to total of firm's net financial debt(after liquid assets and stocks are decreased) and values of the share (Chambers 2009) cited in (Karaca & Savsar, 2012). Firm value is one of the concepts that have been developed for accounting the real value of the firms more realistically considering the concept of market value. Firm value is a concept demonstrating the value of the firm purified from the cash and cash equivalents and financial debts as regards to the concept of market value (Ilgaz, 2010).

2. Statement of the Problem

The listed manufacturing companies in Nigeria do find it difficult to make a profit; this does affect their performance which may be attributed to inadequate finance or where the finance is available at a cost too expensive (Akintoye, 2016; Akinyomi & Olagunju, 2013). The problem of financing decision therefore, arises from determining the equantumo feach source of finance that will yield optimum return with little risks (Akintoye, 2016; Dada & Ghazali, 2016). In Nigeria, one of the fundamental causes of corporate distress points to the fact that inadequate capital, mismatch in finance and inappropriate capital mix characterize the Nigeria firms (Salawu, 2007) cited in (Obboh, Isa & Adekoya, 2012)

Generally, firms are faced with a complex challenges list of options when deciding on their choice of financing decision. Most firms have to choose either to finance their investments with retained earnings, new equity issues, or through debt. However, it has been observed that the Nigerian firms most often use equity rather than debt in financing projects as compared to firms in the developed nations (Adeyemi & Obboh, 2011). There has been a limited number of studies in Nigeria that have examined the firm's choice of financial decisions and its market value, but few researchers gave different view and results on firm's choice of capital structure which include: Obboh, Isa & Adekoya (2012) studied the corporate capital structure and corporate market value in Nigeria. Other research works focused on the capital structure and financial performance of listed manufacturing firms in Nigeria and/or in other countries include, Ajibola et al (2018); Adesina, Nwidobie & Adesina (2015); Akinyomi et al (2013); Dada & Ghazali (2016) and Getahun (2016). However, the review of previous empirical literature revealed a lack of established the influence of financing decision on the firm value of listed manufacturing companies in Nigeria over the period of 2014-2018. None of researchers used the variables of market share price proxy firm value and independent variables of total equity and long term debt to measure financing decision for period of 2014-2018 in their research findings which indicates the existence of a research gap. In view of the above, this research is to evaluate the influence of financing decision on the value of listed manufacturing companies in Nigeria. Hence, this study will provides the shareholders and varying stakeholders, including senior management, managers and policy makers to find of this study useful so as to aid them for an effective and efficient financing decision of firms in Nigeria

3. Research Question

What is the influence of total equity on firm value of listed manufacturing companies in Nigeria?

4. Objective of the study

The objective of the study is to investigate influence of total equity on firm value of listed manufacturing companies in Nigeria

5. Research hypothesis

Total equity has no significant influence on firm value of listed manufacturing companies in Nigeria

6. Literature Review

Conceptual Review

Financing decision is the second important function to be performed by the financial manager. Broadly, financial manager must decide when, where from and how to acquire funds to meet the firm's investment needs. The central issue before financial manager is to determine the appropriate proportion of equity and debt. The mix of debt and equity is known as the firm's capital structure. The financial manager must strive to obtain the best financing mix or the optimum capital structure for the firm (Pandey 2005). The firm's capital structure is considered optimum when the market value of share is maximized. In the absence of debt, the shareholders' return is equal to the firm's return. The use of debt affects the return and risk of shareholders; it may increase the return of equity funds, but it always increase risk as well, The change in the shareholders' return caused by the change in the profits is called the financial leverage. A proper balance will have to be struck between return and risk. When the shareholders' return is maximized with a given risk the market value per share will be maximized and the firm's capital structure would be considered optimum (Pandey 2005). Once the financial manager is able to determine the best combination of debt and equity, he or she must raise the appropriate amount through the best available sources.

In practice, a firm considers many other factors such as control, flexibility, loan covenants, legal aspects etc, in deciding its capital structure. Corporate financing decision deal with amount of capital that is required for a firm to operate and the best mix of capital structure for the firm (Pike & Neale, 2009). To maximize the firm value, all the rational firms will pursue the lowest cost of capital and the optimal capital structure. Firms that have a pertinent blend of debt and equity will benefit the firm in the long run. The build-up of an optimal debt-equity mixture will reduce the cost of capital, and increase in the net economic return and consequently raise the firm's value (Awan, Bhatti, Ali, & Qureshi, 2010) cited in (Chaleeda, Islam, Ahmad & Ghazalat, 2019). Companies fund their investment projects using internal and external funds. Internal financing is whereby companies use non-cash expenses and retained earnings, and external financing refers to the proceeds from new equity and debt issuance. In a capital market world. Internal and external funds are not perfectly substitute, and thus dividends, financing, and investment decisions are related

(Simmons-Suer, 2016). Moreover, firms prefer to use internal funds to finance additional investments rather than issuing new securities because when there are capital market imperfections. Internal funds are cheaper sources of financing.

Equity and firm value

Equity includes paid up capital share-premium, reserves and surplus or retained earnings. Igben (2004) defines paid-up capital as the portion of the called-up capital which has been paid-up by the shareholders. He also describes reserves as amounts set aside out of profits earned by the company, which are not designed to meet any liability, contingency, commitment or diminution in value of assets known to exist at the balance sheet date. Reserves may be voluntarily created by directors or statutorily required by law. Share premium is the excess amount derived from the issue of shares at a price that is above its par value (Samuel et al, 2012)

Firm value

Firm value is the perception of the investor to the success of a company. It is reflected in the share price of the company. The increase of the share price shows the trust of the investors to the company. They are willing to pay more with aiming for a higher return.

The firm value is the total assets owned. It consists of the market value of share and liabilities (Ifada, Faisal, Ghazali, & Udin, 2019). The high stock price can provide a good signal to attract investors to determine investment decisions. The firm value in this study uses proxies of market share price.

Theoretical review

Several theories have been used in examining the relationship between the capital structure and value of a firm, these theories includes the Pecking Order theory, the Trade- off theory, the Net Income Approach, the Net Operating Income Approach, the Modigliani and miller Hypothesis, the Asymmetric Information Approach and the market timing theory. However, this study considered pecking order theory and market timing theory, because when choosing which funds to use in financing, firms first use to consider their internal sources of funds, or retained earnings, then debt, and lastly equity. Using retained earnings involves lower funding costs and shorter processing times compared to debt funding, yet equity funding involves yet higher funding costs and even longer processing times. Therefore, debt financing positively affects firm value in term of market share price. Firms with more profit and liquidity have more retained earnings and do not need external funding. Firms involved in high-risk ventures should not need more debt as more debt means even more financial risk. However, growth opportunities and non current assets positively affect liability. The retained earnings of high growth firms might not match their capital requirements, so they add more debt. Moreover, tangible assets can be used as security when firms

require debt funding.

This Market Timing theory introduces the impact of timing on firm's financial decision making process. It explains that the choice between the use of capital or equity is a function of manager's ability to time the equity market, as firms will prefer using equity so long as the relative cost of equity is low, and if otherwise preference will be on the use of debt instruments (Adu, 2016). Under this approach, the stock market condition play crucial role in explaining the firm's leverage condition, for instance, during bullish equity market, firms prefer equity issuance over debt financing.

Empirical Review

Chaleeda, Islam, Ahmad & Ghazalat (2019) examined the effects of corporate financing decisions on firm value in Bursa Malaysia. They found that there was a consistent with the view that leverage and dividends mitigate agency costs of free cash flow problems, therefore, increasing firm value while total debt to total assets affects firm value negatively. This proves that although there are benefits of debts, there is also the cost of debts. The cost of debt financing arises from the increase in the probability of bankruptcy and firm value does not depend on the length of debt maturity.

Ifada, Faisal, Ghozali, and Udin (2019) investigated the company attributes and firm value in companies listed on Jakarta Islamic index. They disclosed that ownership concentration and profitability have a positive effect on firm value. In contrast, liquidity has a negative effect on capital structure. Finally, capital structure mediates the relationship between profitability, liquidity and firm value.

Maneerat tanarungrot and Donkwa (2018) studied the capital structure affecting firm value in Thailand. They found that tangibility positively affects debt financing and liquidity, risk negatively affects debt financing, and debt financing has no effect on a firm value. They suggested that financial managers could use these results to develop their capital structure to support other operations within the firm

In a similar study, Aggarwal and Padhan (2017) investigated the effect of capital structure and firm quality on firm value of selected BSE listed Indian hospitality firms over a time frame of 2001-2015. They revealed that there was a significant relationship of firm value with firm quality, leverage, liquidity, size and economic growth. Gichuhi (2016) examined the effect of capital structure on profitability of firms listed at the Nairobi securities exchange. It was concluded that there existed an insignificant link relating capital structure and profitability of listed firms. In addition

Asif and Aziz (2016) examined the impact of capital structure on firm value creation evidence from the 20 companies of cement sector in Pakistan quoted on the Karachi Stock Exchange (KSE) for a period of 2006 to 2015. The outcomes of the study represent that most of the debt to equity ratio, return on capital employed, and share capital and current ratio have positive correlation which concluded that Capital Structure has positive impact on firm value.

In addition, Fumani and Moghadam (2015) studied the effects of capital structure of the company value, the rate of return on equity and earnings per share of listed companies in Tehran Stock Exchange during the years 2010-2014. They found that the rate of return on equity has a negative impact significantly on financial leverage. Also, the market values of the company's earnings per share significant effect on the financial leverage it.

Kodongo, Mokoaleli-Mokoteli, & Maina (2014) investigated the capital structure, profitability and firm value of listed firms in Kenya. They employed various panel procedures and annual data for the period 2002-2011. However, leverage has no effect on Tobin's Q proxied for firm value. They further disclosed that the performance of firms depends on other things than just their capital structure. They also revealed that sales growth and firm size are important factors driving firm value (Tobin's Q). Mabururu (2012) assessed the impact of taxes on financing decisions and firm value for companies quoted at the NSE. He concluded that high levels of debt are not good for the value of a firm. This is because at high levels of leverage, agency problems arises between the stockholders and the debt holders as debt is risky creating negative influence on the value of the firm.

Samuel, Ebenezer and Xicang (2012) evaluated the impact of capital structure on a firm's value: Empirical Evidence from Ghana. They found that in an emerging economy like Ghana, equity capital as a component of capital structure is relevant to the value of a firm, and Long-term-debt was also found to be the major determinant of a firm's value. Oboh, Isa and Adekoya (2012) studied the corporate capital structure and corporate market value: Empirical evidence from Nigeria. They concluded that firms' leverage positively influence their market values and suggesting that, a firm can actually attain an optimal capital structure.

7. Methodology

This study adopts the Expo-facto research design. This is because data needed for analysis already exists.

The population of the study consisted of twenty one quoted consumer goods sectors manufacturing firms in Nigerian Stock Exchange as at 2019 while sample size was six quoted selected manufacturing companies for a period of 2014 and 2018. The purposive sampling technique which is a method of non-probability sample was used for this. The lists of all sampled selected companies are as follows: Nigerian Breweries plc, Card-bury plc, Nestle Nigerian plc, Guinness Nigerian plc, International Breweries Plc, Honeywell Flour Mill plc.

The data collected for this study obtained from the secondary source. The data used for analysis were extracted from the audited annual financial reports and accounts of selected manufacturing companies stated above. This study adopted the descriptive statistics and Ordinary Least Square OLS technique- Linear Regression Analysis using E-view 9 version.

Operational variables

Dependent variable	Operational definition
Firm value proxy by market share price (MSP)	Is the price of share exchange quotation at financial year end
Independent Variable	
Total Equity	This includes paid up capital share-premium, reserves and surplus or retained earnings

Source: Researcher's Design (2020)

Model Specifications: The model of study was established the relationship between the dependent variable firm value proxy as (MSP) and total equity through the model adapted from work of (Akinyomi & Olagunju, 2013).

MSP Model

This model shows the significant relationship between MSP and TEQ The model is specified on the functional and stochastic form.

$$MSP = f(TEQ, \mu) \dots \dots \dots \text{eg.1}$$

$$LMSP = \alpha + 1L TEQ_{it} + \mu \dots \dots \dots \text{eg.2}$$

Where, α = Constant Parameter 1 = Regression Coefficient of Variables MSP = market share price, TEQ

= Total Equity

Log L = Natural logarithm of the variables, U_{it} = Error terms Note the subscription index "it": I = i^{th} Cross sectional unit, I = 1, N

t = t^{th} time period, $i = 1, \dots, T$ A priori Expectations: +/-

8. Results and Discussion

Table 4. 1 provides the summary of descriptive statistics of LMSP and LTEQ, for the study. As shown in table, the sum, mean, maximum and minimum, standard deviation and variance as well as the skewness and kurtosis of the variables of interest are evident. The various statistics indicate that, the variables have different distributions. The skewness and kurtosis statistics provide useful information about the symmetry of the probability distribution of various data series as well as the thickness of the tails of these distribution respectively from the result analysed in table 4.1 showed the average value of the series which is obtained by dividing the total value of the series by the number of observations. The table showed that the mean for LMSP and LTEQ are 1.685 and 7.555 respectively. From the table, LTEQ had a maximum value of 8.250 and a minimum value of 7.04. The implication of this is that LTEQ contributed maximally to the increased value of firm during the sample period

Table 4.1 Description Statistics of the model

	LMSP	LTEQ
Mean	1.685333	7.555000
Median	1.760000	7.570000
Maximum	3.190000	8.250000
Minimum	0.020000	7.040000
Std. Dev.	0.886845	0.400187
Skewness	-0.052170	0.379654
Kurtosis	2.216764	2.135576
Probability	0.676910	0.437202
Sum	50.56000	226.6500
SumSq. Dev	22.80835	4.644350
Observations	30	30

Table 2: showed that total equity had a significant positive relationship with the market share price ($r = .377$, $p < .01$), indicating that total equity had significant influence on market share price. The correlation coefficients were at 1% level of significance.

Table 4.2: Pearson's Correlation Matrix

	Market Share	Total Equity
Pearson correlation	1	.377**
Market share Sig. (2-tailed)		.007
N		50
Pearson Correlation	.377**	1
Total equity Sig. (2-tailed)	.007	
N	50	50

**Correlation is significant at the 0.01 level (2-tailed).

From the table 4.3 it was observed that the coefficient of determination for the regression as depicted by the R^2 value of 0.16 suggest that about 16 percent

Of the systematic variation of the dependent variable is accounted for by the explanatory variable. The remaining 84 percent is caused variable that are not included in the model which is accounted for by the stochastic error term. The F- statistics of 5.489 shows that the model of the study is well fitted; this can be confirmed by the significant value of 0.02 which shows the null hypothesis is rejected, this implies that there is a significant relationship between total equity and firm value of manufacturing companies. However, it was also discovered that variable of total equity has positive influence and statistical significant impact on MSP as confirm P- value < 0.05 . This means as equity capital increase, firm value also increases. Specifically from the table 4.3, a unit increases in equity will lead to a corresponding increase in firm value by .879 units. This means that equity is positively related to the

firm value of listed manufacturing firms in Nigeria. Theoretically, the evidence of a positive effect of equity on firm value reveals the presence of the market timing theory in the financing behaviour of firms.

Table 4.3

Dependent Variable: LMSP

Method: Panel Least Squares

Date: 03/26/20 Time: 18:42

Sample: 2014 2018

Periods included: 5

Cross-sections included: 6

Total panel (balanced) observations: 30

Variable	Co efficient	Std. Error	t-Statistic	Prob.
C	-5.092832	2.897053	-1.757936	0.0897
TEQ	0.897176	0.382943	2.342847	0.0265
R-squared	0.163903	Mean dependent var		1.685333
Adjusted R-squared	0.134042	S.D.dependant var		0.886845
S.E of regression	0.825270	Akaike info criterion		2.518129
Sum square resid	19.06999	Schwarzcriterion		2.611542
Log likelihood	-35.77194	Hannan-quinnccriter.		2.548013
F-statistic	5.488932	Durbin-Watson stat		0.128311
Prob(F-statistic)	0.026472			

Source: Author's computation (2020)

The study investigated the influence of total equity on firm value of manufacturing companies in Nigeria. This variable was regressed on market share price (MSP). The total equity contributes positively and statistical significant to the MSP. This is because equity capital as a component of capital structure that is relevant to the value of a firm.

From the above results, it can be seen that total equity has significant impact on market share price of manufacturing companies. This finding is in line with Samuel et al (2012) reported that equity capital as a component of capital structure is relevant to the value of a firm. This conforms to the research work of lawal (2014) who found that equity role is partially significant to firm value. The findings also corroborated to the study of Oboh et al (2012) found that there was a significant and positive relationship between non-financial firms' market values and their debt equity ratios. This study also consistent with Adu (2016) who found that equity is positively related to the firm value of listed manufacturing firms in Ghana.

9. Conclusion and Recommendations

This study examines the influence of financing decision on firm value of listed manufacturing companies. Data were obtained from six selected manufacturing firms with a total 30 observations. The results of the analysis revealed that financing decision (a measure of equity) has a positive relationship with firm value.

In the view of above findings, it could be concluded that variable of total equity has positive influence and statistical significant impact on firm value proxy by market share price. Based on the findings of this study, the study suggested that firms should time the equity market to determine when equity capital becomes cheaper as compared to debt capital. However, as suggested by the market timing theory, equity capital may only be beneficial in some periods. Listed manufacturing firms should exhaust their retained earnings before they can decide to utilize other forms of investment such as debt and leverage. This will ensure maximize utilization of available funds and accurate choice of investment while maximizing wasteful spending

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