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Abstract

The capital structure is a combination of different types of debt and capital which a firm uses to finance its assets, operations and growth. This study critically examined the relationship between capital structure and firm's performance. Capital structure is a dynamic process that changes depending on the variable that influence evolution or performance of a company. Appropriate capital structure decision is one of the most crucial decision often confronted by financial managers and analysts of firms. Capital structure plays an important role in a firm especially when the firm wants to fulfil the needs of their stakeholders through investments in capital assets, profitability, payment of dividend, debt, salaries on time and other financial obligations. Capital structure is normally made of equity capital, preference capital and long-term debt capital. Debt capital such as long-term bond is used by the firm to finance mainly its investment decision in long term assets

such as property, plant and equipment. The decision centers on the mix of debts and equity in financing firm's immediate and long term assets and operations. The combinations of different capital types will have differing impact on firm performance. Capital structure is used as a benchmark when raising funds for investment in new capital projects. Managers have numerous opportunities to exercise their discretion with respect to capital structure decisions. The capital structure employed may not be meant for value maximization of the firm but for protection of the manager's interest especially in organizations where corporate decisions are dictated by managers and shares of the company closely held. The managers are caught up in a dilemma of structuring their finance in order to determine its impact on performance. The performance of the business is crucial to the value of the firm and consequently, its survival. The question firms are faced with is making a decision on the capital structure choice to use. The decision is crucial given that it has effect on the financial performance of firms. The capital structure of a firm is generally the specific mix of debt and equity the firm uses to finance its operations. The paper sought to assess the relationship between the capital structure and performance. The paper is anchored on agency cost theory and supported by the static trade-off and the pecking order theory. The paper revealed that financial leverage has a positive and significant effect on firm performance. The paper further reveals that there is positive relationship between capital structure and financial performance. Capital structure was found to have a significant effect on financial performance of the firm. The paper concludes that every firm should make good capital structure decision to earn profit and carry on their business successfully.

Keywords: *Capital structure, Debt, Debentures, Equity, Leverage, Financial performance*

Introduction

Capital structure decisions are one of the three financing decisions namely investment, financing, and dividend decisions that finance managers have to make (Karadeniz, Kandir, Balcilar, & Onal, 2009). The capital structure of a firm is actually a mix of different securities. In general, a firm can choose among many alternative capital structures. It can issue a large amount of debt or very little debt. It can arrange lease financing, use warrants, issue convertible bonds, sign forward contracts or trade bond swaps. It can issue dozens of distinct securities in countless combinations; however, it attempts to find the particular combination that maximizes its overall market value (Liang, Li, & Song, 2014). In reality, establishing an optimal capital structure is a difficult task (Shoaib, 2011). He contends that a firm may require issuing a number of securities in a mixture of debt and equity to meet an exact combination that can maximize its value and having succeeded in doing so, the firm has achieved its optimal capital structure. Jensen and Meckling (1976) demonstrates the amount of leverage in a firm's capital structure affects the agency conflicts between managers and shareholders and thus, can alter managers' behavior and operating decisions. This position is supported by Ebaid (2009). The existence and achievement of an optimal capital structure is of great concern for investors and management of firms.

Capital structure has attracted a lot of debate and academic attention across industries in the corporate finance literature over the past decades and continues to engage the attention of researchers (Niresh, 2012). The importance of the subject matter stems from the fact that capital structure affects the profitability of corporate entities irrespective of their industry. Capital structure is simply defined as the combination of debt and equity that achieves the stated managerial goal of maximizing the value or wealth of shareholder. The wealth of shareholders in turn is measured by the current price of the firm's shares. In order to achieve this objective, firm's

management should take rational financing decisions regarding optimal capital structure which in turn would minimize its cost of capital (Goyal, 2013). The mixture of debt and equity that will achieve the above objective is the optimal capital structure. Capital structure studies have been inspired by the pioneer work by Modigliani and Miller (1958).

The authors at the time argued that a firm's choice of capital structure does not have any positive effect on firm value. This argument was made on the assumption that there are no taxes, no transaction costs; there is symmetric access to the credit market etc. Since then, three different theoretical explanations on the subject have been developed: the Static Trade-off, the Pecking Order and the Agency Cost theories (Buferna, Bangassa & Hodgkinson, 2005).The Static Trade-off theory argues that an optimal capital structure is obtainable; where the tax benefit of debt financing is equal to the leverage associated costs which may include financial distress and bankruptcy while investment decision and firm assets are held constant (Chechet & Olayowola, 2014). The Pecking Order theory posits that the optimum capital structure is difficult to determine because firms make use of first internal financing, then external financing in the form of debt and debentures in financing new investments. Equity capital appears both at the start and end of the pecking order. The Agency Cost theory lastly states that an optimal capital structure is attainable by reducing the costs resulting from the conflicts between the managers and the owners. Jensen and Meckling (1976) posit that leverage level can be used to monitor the managers to pursue the overall firms' objectives and not theirs. By so doing, cost is reduced leading to efficiency which will eventually enhance firm performance (Buferna *et al.*, 2005). Capital structure has become one of the most researched areas in both the theoretical and empirical literature in finance (Hossain & Hossain, 2015).

Capital structure

Capital structure is the combination of debt and equity used to finance firm's assets, operations and growth. A firm can be financed by the shareholders or debt holders or hybrid (Umar, Tanveer, Aslam & Sajid, 2012). If financed entirely by share subscription then the entire profits go to the shareholders. If financed by both debt and equity then the profit is shared. If the value of the firm can be affected by capital structure or financing decision, a firm would like to have a capital structure which maximizes the market value of the firm. An optimal capital structure and how to calculate one that maximizes a firm's profits has remained elusive to date. A great dilemma for management and investors alike is whether there exists an optimal capital structure and how it influences financial performance (Umar *et al*., 2012).

Financing of all firms is done by equity, debt or hybrid security. In their study on the relationship between capital structure and financial performance of one hundred companies in Pakistan (Umar *et al*., 2012) found out that all the three variables of capital structure, current liabilities to total asset, long term liabilities to total asset, total liabilities to total assets negatively impacts the earnings before interest and taxes, return on assets, earnings per share and net profit margin (Nirajini & Priya, 2013). What is known as financial structure is the product of different factors from inside and outside the company. It is probable that internal factors are affected by outside determinants which can be observable through the companies' leverage similarities within an industry (Nejad & Wasiuzzaman, 2013).

Akintoye (2009) confirmed the role of business risk, taxes, managerial behavior or financial flexibility in the analysis of firm performance. According to Akintoye (2009), the capital structure is based on the trade-off between risk and expected return, these are crucial factors in determining

target capital mix. This target would guide companies towards an ideal mix of debt and equity that minimizes the cost of capital and maximizes the company value. Moreover, any changes made in the level of debt or equity will modify the firm's value. According to tax benefits, it is expected that under the tax burden, companies would borrow more in order to achieve a higher performance. Some think that performance is the total market value of a firm or the sum between market value of equity and value of equity options (Merz & Yashiv, 2007). A firm's performance reflects how effectively companies manage their resources. There is a multitude of capital structure indicators that influence the firm performance and profitability.

Capital structure involves different sources of long term capital through which an enterprise finances its assets (Kirmi, 2017). Capital structure influences both shareholders' return and the ability of a firm to survive economic depression (Joshua, 2017). Mohammad and Jaafer (2012) states that firms can use either equity or debt to finance their assets. But where the interest was tax deductible, firms would maximize the value accruable by using more debt. Equity capital refers to shareholders contribution, such as common stock. The debt capital in a firm's capital structure refers to borrowed monies, such as bonds, loans, debenture, and commercial papers. Capital structure decision becomes relevant to any business enterprise which has the need to maximize shareholders' return and achieve competitive advantage. The mix/ratio of debt and equity in the company's mode of financing refers to capital structure. Some organizations prefer more debt while others prefer more equity in financing their assets.

Source of capital refer to the place or platform where financial resources can be acquired. A firm can source for fund; either internally or externally or both, which constitute the firm's structure of capital (Zunckel & Nyide, 2019). Structure of capital refers to the blend of firm's financial liability (Uremadu & Onyekachi, 2019). It could be seen as the debt and equity mixture that the firm has employed to finance business operation (Aziz & Abbas, 2019). Structure of capital is the sum of debt and equity quantum or preference shares, common stock and other debt obligations. Irrespective of the industry, as business expands, capital requirement also increases, thus it needs funds which can come from any of these source (debt, equity or combination of both). The source of fund must be considered based on cost-benefit. A preferred source of fund to an organization should lead to more profitability to the firm than other sources of funding.

Financial leverage occurs through fixed financial expense on the firm which bears a fixed interest payment (Adenugba, Ige & Kesinro, 2016). Financial leverage is a debt incurred by a firm from financial institutions with the intention that such investment will earn more than the cost of interest charged on the debt (Abubakar, 2015). Additionally, financial leverage employed by a firm is motivated by the intention of earning higher returns on debt than the weighted cost (Enekwe, Agu & Eziedo, 2014). The possible outcomes with the use of financial leverage can be profit maximization or minimization. Thus, the high debt level which should be paid at a cost exposes the firm to risk (Al-Otaibi, 2013). Financial performance analysis deals with the following items: capital employed, asset base, sales turnover, dividend growth (Omondi & Muturi, 2013). Financial performance is expressed by increase in stock prices, sales, profits and dividend (Maghanga & Kalio, 2012).

Many authors have suggested a positive relationship exists between a firm's leverage and its size (Fama & French, 2002). Warner (1977) and Ang, Chua and McConnell (1982) stressed, that when the value of the firm increases; the ratio of direct bankruptcy costs to the firm value would decrease. On the other hand, smaller firms face a different reality in raising the long term debt. Asymmetric information is not the main reason, but the reason is the significant negative

correlation between firm size and the probability of bankruptcy (Hall, Hutchinson & Michaelas, 2004). One explanation could be that relatively large firms tend to be more diversified; therefore, they are less prone to insolvency (Titman & Wessels, 1988). Chittenden, Hall and Hutchinson (1996) stated that the cost of monitoring large companies is much lower than small firms.

Corporate organizations can raise more funds through long-term finance sources than a sole proprietorship. The age or duration of business operation determines the firm's ability to accumulate retained earnings which form part of its capital structure (Ezenwakwelu 2017). The longer a firm continues in business, it establishes the capacity to take more debt (Myers, 1977). Business size determines the ability of raising funds by an organization. People subscribe to a firm's share capital if they know the size of the business and prospects of its success. The larger the firm, the more possible it can issue debt and lower the risk of bankruptcy (Titman & Wessels, 1988). Warner (1977) posits that a large firm would have lower transactions costs of external financing than a small firm, making it difficult for the small firms to acquire debt and therefore preventing them from utilizing external financing. Generally, big firms have diversified business strategy, which enables them to have stable earnings that reduce the risk of bankruptcy and contribute in meeting their debt obligations (Marsh, 1982). Firms raise debt at cheaper rates if they have large amount of fixed assets. Such firms have an incentive to obtain loans at cheaper rate. Firms with large amount of fixed assets would secure higher level of debt. Corporate organizations consider their liquidity position before embarking on the issue of debenture or debt issuance. This prevents bankruptcy or being unable to pay debts. A firm is said to be liquid when it has the ability to generate cash required in servicing its debt obligations. Cost of capital is considered by firms when raising funds. Experience gathered by firms proved that the cost of debt is lower than the cost of equity capital because firms usually borrow debt capital at a cost less than it earns. Also, interest charges for borrowing funds are tax deductible. An increase in debt ratio results in increased variability in income. The desire of a firm to have control of the organization may determine the finance source the firm may use. Thus, the firm may prefer debt issues and preferred stock to common stock (Ezenwakwelu, 2017).

Performance

The result of a firm's performance is the output where the stakeholders hope for a positive outcome. One of the debatable issues in finance is regarding the idea or concept of performance due to its multi-dimensional meanings (Zeitun & Tian, 2007). Study related to firm's performance originates from organization theory and strategic management (Murphy *et al*. 1996). Performance measure can be divided into two categories which are financial performance or organizational performance. Profit maximization, maximizing profit on assets and maximizing shareholders' value are examples of measurement for financial performance. The financial performance of a firm is a mathematical measure that evaluates how well it is using available resources to make profit. A review of literature reveals that the financial performance has been basically measured using three approaches: market, accounting, and survey measurements (Masa'deh *et al*., 2015). While the first approach reflects the degree of satisfaction of the shareholders, the second captures internal efficiency of the firm while the last performance measurement approach provides subjective estimation of a firm's financial performance. On the other hand, operational performance such as growth in sales and growth in market share referring to a wide definition of performance since they focus on determinants that contribute to financial performance (Hofer & Sandberg, 1987).

Capital Structure and Performance

The determination of a firm's optimal financial structure is a difficult one since it involves an analysis of several factors, key among them risk and profitability (Shubita & Alsawalhah, 2012). The decision becomes even more difficult, in times when the economic, social, technological and political environments in which the firm operates exhibits high degree of instability (Shubita & Alsawalhah, 2012). Therefore, the choice among ideal proportion of debt and equity can affect the value of the company, as well as financial performance. Indeed, Chiang, Chan and Hui (2002) study at Hong Kong Stock Exchange (HKSE) concluded that financial performance as measured by profitability and capital structure, a subset of financial structure, are interrelated. Many firms therefore fail for not putting proper strategies, financial among others, in place. Factors contributing to business failure can be addressed through proper strategies to drive growth and achievement of organizational objectives (López Salazar, Contreras Soto & Espinosa Mosqueda, 2012). It is necessary and sufficient that proper care and attention be given while making financial structure decision which otherwise can cause financial distress (Singh & Faircloth, 2005). Options could be several but to decide the best choice in firm's interest in a particular scenario needs somebody to have a deep understanding in the field of finance to critically analyse the impact of the available options on the firm's performance.

For instance, while some researchers like Gill, Biger and Mathur (2011) have put it that use of more proportion of debt in capital structure can be effective as it is less costly and has a positive relationship with profitability (a proxy for financial performance) than equity others like Chechet and Olayiwola (2014) have argued that equity capital is preferred. Majumdar and Sen (2010) examined the role of different types of debt on the strategic behaviour and performance of firms in India. The results showed that the debt types have significant relationship with performance. The results also reveal that the debt structure matters, and it is important to take into account institutional differences and the heterogeneity of debt in the analysis of capital structure on firm performance.

In a related study, San and Heng (2011) investigated the relationship between capital structure and performance of Malaysian firms in the construction sector before and during crisis that started since 2007.The results indicated that return on capital was found to be positively related to debt to equity market value for big firms. The same positive relationship was found between earnings per share and long term debt to capital. However, earnings per share were found to be negatively related with debt to capital. They also reported that operating margin and long term debt to common equity were positively related for medium companies and earnings per share and debt to capital has negative relationship in small companies.

Salim and Yadav (2012) analyze the effect of capital structure on performance of listed firms. The results indicated that capital structure measured by total debt and short term debts have negative impacts on ROE. This result is consistent with Ebaid (2009). Long term debt and Total debt as measure of capital structure has negative impact on the performance of firms when it was measured by ROA. This supports the findings of Zeitun and Tian (2007) and Abor (2007) that indicate that performance is negatively related to capital structure. The study also found that Tobin's Q has positive and significant impact on short term debt, long- term debt and total debt. A recent study by Fosu (2013) analyzes the effect of capital structure on firm performance with focus on the degree of product market competition of South African firms. The findings reveal that financial

leverage has a positive and significant effect on firm performance and product market competition helps in enhancing the performance effect of leverage of South African firms. More recent studies by Oino and Ukaegbu (2015) on Nigeria firms indicated that profitability is negatively related to leverage. However, a current study by Bandyopadhyay and Barua (2016) on capital structure and firm performance in India indicated that macroeconomic cycle significantly influences capital structure choice of firms which in turn affect their performance.

Nassar (2016) ascertained the effect of capital structure on financial performance in Borsa Istanbul stock exchange between 2005 and 2012 with multivariate regression analysis in measuring return on asset, return on equity and earnings per share as firm performance indicators and debt ratio as a proxy of capital structure. The results show that, there is a negative significant relationship between capital structure and firm performance. Uremadu and Onyekachi (2019) studied the effect of capital structure on corporate performance in Nigeria. The study employed return on asset, long term debt to asset ratio and total debt to equity ratio. The results from the research found a negative and insignificant impact of capital structure on corporate performance of the consumer goods firm sector of Nigeria. Aramvalarthan, Kannadhasan, and Babu (2018) investigated the dependence among capital structure and corporate in India with the application of panel data method in measuring the link between return on equity, firm size, tangibles and capital structure. The result shows that financial leverage has a positive significant effect on the financial performance of the firm. Aziz and Abbas (2019) ascertained the association of different debt financing on firm's performance in fourteen economic sectors of Pakistan from 2006 to 2014 with the use of regression method. The results of the study indicated that debt financing have negative but also significant impact on firm performance in Pakistan.

Dada and Abbas (2016) examined the effect of capital structure on firm performance by measuring asset turnover, tangible asset and return on asset in selected firms in Nigeria between 2010 and 2014. The results from the panel data approach shows that assets turnover and tangible assets have a significant positive relationship with Tobin's Q. Risk indicated a significant negative association with Tobin's Q. Age on the other end had a significant negative link with ROA and Sales growth indicated a significant positive association with return on asset. Muigai and Murithi, (2017) ascertained the moderating effect of firm size on the association between firm's capital structure and financial distress of non-financial firms in Kenya from 2006 to 2015 with feasible generalized least square regression model. The results from the study showed that firm size has a significant moderating effect on the relationship between capital structure and financial distress of non-financial firms. Mulyana, Zuraida, and Saputra, (2018) evaluated the impact of profitability, liquidity and leverage on earnings and its effect on the value of firms in Indonesia stock exchange between 2011 to 2015. The study employed hypothesis testing on secondary data of 150 manufacturing organizations.

Shen (2017) empirically investigated the association between capital structure and corporate performance in China from 2011 to 2015 with regression method in analyzing return on equity, return on asset, gearing ratio, long term debt capital ratio and current debt capital ratio. The research found a weak degree of negative correlation between asset liability ratio and performance of listed companies in China. Cheema, Mahboob, Farooq, and Yousaf (2017) investigated the link between capital structure and financial performance of Shariah and non Shariah companies in Pakistan between 2009 and 2015 with multiple regression method. Dependent variable measured by ROA and ROE while capital structure as the explained variable measured by long term debt ratio, short term debt ratio, and sales growth ratio non-debt tax shield and inside holding. Results

from the multiple linear regression and correlation revealed that capital structure affect the performance of a firm in the case of non-Shariah companies but do not significantly affect performance of Shariah companies. Kehinde (2014) conducted the study to explore the relationship between capital structure and survival dynamics of business organization, using multiple linear regression technique. Dependent variable was measured by equity and debt while independent variable was measured by dividend. The study concluded that firms should improve on their capital structure with a mix of debt and equity for effective growth and expansion. Gharaibeh, (2015) embarked on the research to find out the impact of capital structure on the financial performance of listed companies in the Bahrain Bourse from 2009 to 2013. The study employed ROE, ROA, EPS and dividend yield as firm financial performance indicators and capital structure as explained variable. Ordinary least squares method was utilized to ascertain the impact of capital structure on the ROE, ROA, EPS and dividend yield. Capital structure represented by total liability to total assets have positive significant effect on ROE but have no significant impact on ROA, EPS and dividend yield. The results also revealed that lagged performance measures of ROE, ROA, EPS, and dividend yield have positive significant effect on the current year's firm performance.

Dai (2017) determined the link between capital structure and performance of banks in Thailand from 1997 to 2016 with the application of random effect model in measuring capital structure, size, growth, credit risk and liquidity risk. Evidence from the results proved significant and negative association between capital structure and profitability of Thailand banks which implies that pecking order theory was valid for the period and data set employed. Akingunola, Olawale and Olaniyan, (2017) examined the link between the decision on capital structure and organization's financial performance in Nigeria between 2011 and 2015. Short and long term debt had positive significant effect on ROE and ROA for the study period. Dang, Bui, Dao and Nguyen, (2019) investigated capital structure and its relationship with firm financial performance concentrating on Food and Beverage firms in Vietnam. The results indicated that financial leverage has a strong influence on firm financial performance; debt ratios positively and significantly influenced earnings per share and return on equity but influenced return on asset negatively.

Ganiyu, Adelopo, Rodionova and Samuel (2019) examined the association between capital structure and firm performance in Nigeria. The study employed total leverage ratio, long term leverage, short term leverage, asset tangibility, growth opportunity, risk, ownership, age, size and return on equity as variables. The research found a significant relationship between capital structure and firm financial performance. The above empirical findings also revealed issues surrounding capital structure and firm financial performance which have been widely debated in the finance literature, yet there has been no conclusion as to how composition of firm‘s capital influences firm's financial performance. Studies such as Nassar (2016); Uremadu and Onyekachi, (2019); Aziz and Abbas, (2019); Shen, (2017) found a negative relationship between capital structure and firm performance while Aramvalarthan, Kannadhasan and Babu (2018); Gharaibeh, (2015); Ganiyu, Adelopo, Rodionova, and Samuel (2019); Dada and Abbas (2016) found a significant positive relationship between capital structure and firm performance.

Sultan and Mustafa (2015) investigated the effect of capital structure on profitability among listed firms in Iraq and employ OLS regression analysis on panel data from firms within the industrial sector for the period (2004-2013). The study concluded that total debt ratio positively and significantly affects ROA and ROE in the sample. Sorana (2015) examined the relationship between capital structure and financial performance in 196 Romanian companies listed on the Bucharest Stock Exchange and operating in the manufacturing sector, over a period of eight-years

(2003-2010). Results of this study reveal that ROA is significantly and negatively affected by total debt (TD) ratio. Similar results have been reported by Chakraborty (2010) from an analysis of the determinants of capital structure of Indian firms using a panel of 1169 non-financial firms listed in either the Bombay Stock Exchange over the period 1995–2008 as well as Cheng's (2009) study of the relative effects of debt and equity financing on the operating performance of Taiwanese listed companies over the period from 1995 to 2004. Additionally, Bokhari and Khan (2013) found a negative relationship between total debt and ROA and ROE among Pakistani's non-financial sector firms. Mwangi, Makau and Kosimbei (2014) investigated the relationship between capital structure and performance among 42 non-financial companies listed at Kenya's Nairobi Securities Exchange covering the period 2006 - 2012. Analysis of panel data through feasible generalised least square (FGLS) regression techniques revealed that financial leverage was significantly and negatively associated with ROA and ROE.

Discussion

Despite the convincing evidence of the financial crisis' impact on capital structure the industry-specific effects are still not confirmed. It is reasonable to believe that the financial crisis' impact on specific industries' capital structure differs since several researchers prove that the capital structure differs between industries (Bradley, Jarrell & Kim, 1984; Frank & Goyal, 2009). Essentially, it is argued that firms operating in the same industry are similar to each other and face similar challenges, risks, profitability, regulations etc., which affect their financial decisions (Bradley et al., 1984; Harris & Raviv, 1991; Kovenock & Phillips, 1995; Frank & Goyal, 2009; Morri & Cristanziani, 2009). The latter reasoning indicates that different industries should be characterized by different capital structures and therefore the effect of the financial crisis may have varied effect among the industries. Moreover, it is evident that theories on capital structure developed so far do not emphasize the direct relation between industry performance and capital structure (Abdullah et al., 2012). As such, this is an area that still can be considered to be vague and blurred. Although there are a lot of researches around capital structure, the importance of the capital structure choice is still equivocal. Viviani (2008) emphasizes the importance of determining the proper amount of debt and equity capital since it enables a company to increase its market value and maximize its returns. However, the findings of capital structure's impact on firm performance are ambiguous. Researchers as Berger and Di Patti (2006), Margaritis and Psillaki (2010) and Fosu (2013) declare that financial leverage has a positive impact on firms' performance.

The explanation lies primarily in the fact that financing the operations with owners' capital is proven to be more expensive than financing through borrowed funds. The reason is that the owners' required rate of return on their invested capital often exceeds the interest rates on loans (Ong &Teh, 2011; Salim & Yadav, 2012). Modigliani and Miller (1963) further argue that companies can utilize debt financing and benefit from leverage since the tax regulations enables debt-financing firms to benefit from the interest deduction. In contrary, scholars as Fama and French (1998) and Gleason, Mathur and Mathur (2000) find a negative impact of financial leverage on firms' performance. The underlying reason is the increased interest expenses on debt that in turn can reduce a firm's performance and thereby increase the financial risk in terms of bankruptcy (MacKay & Phillips, 2005; Brealey, Myers, Allen & Mohanty, 2012; Ross et al., 2013). Also, firms that generate high earnings and are considered profitable are the ones in less need of debt since they can finance investments internally (Boadi, Li, Y., & Lartey, 2015).

Extant literatures on the relationship between capital structure and firm performance yield contradictory results (Phillips & Sipahioglu, 2004; Singh & Faircloth, 2005; Chathoth &Olsen, 2007; Jermias, 2008). Previous studies report a positive relationship between short-term debt and total debt and performance, but a negative impact from long-term debt to profitability expressed through return on equity (Abor, 2007). A negative correlation between leverage and performance, described by the ratio of earnings before interest and tax to total assets, was found in the Chinese firms (Chakraborty, 2010). There are also studies such as Ebaid's (2009), where no significant impact was found between capital structure choices and performance. Studies analyzing the impact of financing decisions on performance and profitability usually employ some of the most relevant capital structure determinants. Besides, in order to avoid risks, profitable companies and those retaining high liquidities avoid leverage (Serghiescu & Vaidean, 2014).

Conclusion

This paper has been completed with the important objective on whether the capital structure affects the financial performance of an organization. The paper reveals that the financing decision is one of the most important roles played by a modern financial manager as they determine the value of a firm. An optimal capital structure is defined as one that will minimize a firm's cost of capital, while maximizing its value. The managers find it hard to choose the amount of debt and equity in their capital structures. The capital structure decision that gives the most optimal value is the one with optimum weighted average cost of capital. This is so because it best maximise firms' value. An appropriate mixture of debt-equity should be undertaken by the firms so as to optimize their capital structure. Firms should put into consideration a suitable choice of capital structure and its effects on performance since it affects the shareholders risks, returns and cost of capital. The financing or capital structure decision is significant managerial decision, as it influences the shareholder return and risk. Finally, the paper concludes that there is positive relationship between capital structure and financial performance. Additionally, capital structure has a significant effect on financial performance of the firm, therefore every firm should make good capital structure decision to earn profit and carry on their business successfully.

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