Investigating the Impact of Capital Structure on Financial Performance of Companies Listed on the Tehran Stock Exchange

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Abstract: *This research examines the impact of capital structure on the financial performance of companies listed on the Tehran Stock Exchange from 2018 to 2022. Using panel data regression models, the study investigates how debt and equity ratios, along with firm size, influence financial performance measured by Return on Assets (ROA). The results indicate that a higher debt ratio negatively affects financial performance, while a higher equity ratio and larger firm size have positive effects. The study employs various diagnostic tests to ensure the robustness of the findings and offers practical recommendations for optimizing capital structure. These insights are valuable for investors, managers, and policymakers seeking to enhance financial performance and stability.*

Keywords: *Capital Structure, Financial Performance, Tehran Stock Exchange, Panel Data Analysis.*

I.   Introduction

Financial performance refers to the measure of a company's profitability, efficiency, and overall financial health. It is typically evaluated through key financial metrics such as Return on Assets (ROA), Return on Equity (ROE), profit margins, and earnings before interest and taxes (EBIT). These indicators provide insights into how effectively a company utilizes its resources to generate profit and manage costs. Strong financial performance is often associated with increased shareholder value, improved cash flow, and enhanced competitive advantage, reflecting a company's ability to sustain and grow its operations.

In an ideal scenario, the impact of capital structure on financial performance would be optimized such that companies strategically balance their debt and equity to enhance their profitability and financial stability. Firms would carefully select their financing mix, leveraging debt to capitalize on tax advantages while using equity to maintain financial flexibility and reduce bankruptcy risk. Such an optimal capital structure would lead to high returns on equity

and assets, stable cash flows, and minimal financial distress, thereby maximizing shareholder value and fostering sustainable growth.

Several obstacles may hinder the achievement of the ideal capital structure scenario. High levels of debt can lead to increased financial risk, potentially resulting in higher interest expenses and a greater likelihood of default during economic downturns. Additionally, market conditions, such as fluctuating interest rates and economic instability, can affect the cost and availability of financing. Agency costs, where the interests of shareholders and management may diverge, can also prevent optimal capital structure decisions. Furthermore, regulatory constraints and limitations on financial flexibility can impede firms' ability to adjust their capital structure as needed.

To achieve the ideal capital structure scenario, companies must adopt a strategic approach to financing. This includes conducting thorough financial analysis to determine the optimal mix of debt and equity based on their risk tolerance and growth objectives. Companies should also regularly review and adjust their capital structure in response to changing market conditions and financial performance. Implementing robust financial planning and risk management practices, along with transparent communication with stakeholders, can further support the pursuit of an optimal capital structure.

Main Research Question:

How does the capital structure of companies listed on the Tehran Stock Exchange affect their financial performance?

Understanding the impact of capital structure on financial performance is crucial for both investors and management. For investors, it provides insights into how financing decisions influence profitability and risk, helping them make informed investment choices. For company management, it highlights the significance of strategic financing decisions in enhancing financial health and achieving long-term growth. Research in this area can offer valuable guidance on optimizing capital structure to improve financial outcomes and support sustainable development.

This research is significant as it provides empirical evidence on the relationship between capital structure and financial performance in the context of companies listed on the Tehran Stock Exchange, a relatively under-researched market. The innovation lies in its application of panel data analysis to investigate this relationship, offering a more nuanced understanding of how

different components of capital structure interact with financial performance over time. This approach contributes to the existing literature by providing context-specific insights that can inform both academic research and practical financial decision-making.

Research Hypotheses:

Hypothesis 1: There is a significant negative relationship between the debt ratio and financial performance (measured by ROA) of companies listed on the Tehran Stock Exchange.

Hypothesis 2: There is a significant positive relationship between the equity ratio and financial performance (measured by ROA) of companies listed on the Tehran Stock Exchange.

Hypothesis 3: Firm size moderates the relationship between capital structure and financial performance, with larger firms showing a different impact compared to smaller firms.

Scientific Objectives:

Objective 1: To determine the impact of debt ratio on the financial performance (ROA) of companies listed on the Tehran Stock Exchange.

Objective 2: To assess the effect of equity ratio on the financial performance (ROA) of companies listed on the Tehran Stock Exchange.

Objective 3: To examine how firm size influences the relationship between capital structure and financial performance in companies listed on the Tehran Stock Exchange.

This research focuses on companies listed on the Tehran Stock Exchange from 2018 to 2022. The study examines financial data for 167 companies selected through a systematic removal approach to ensure data consistency and completeness throughout the specified period.

The findings of this research have practical applications for various stakeholders. Educational institutions can utilize the insights to enhance financial management curricula and provide students with real-world examples of capital structure decisions. Executive bodies and policymakers can use the results to design frameworks that promote optimal capital structure practices among listed companies. Additionally, financial analysts and investors can apply the

findings to make more informed decisions regarding investment strategies and risk management.

II. Literature Review

Capital structure is a pivotal aspect of corporate finance, referring to the mix of debt and equity a company uses to fund its operations and growth. The optimal capital structure balances the cost of capital with financial risk, significantly influencing a company's overall financial performance. Understanding this balance is crucial for investors, managers, and financial analysts as it helps guide financing decisions and strategic planning.

The primary components of capital structure are debt and equity. Debt financing involves borrowing funds that need to be repaid with interest, including loans, bonds, and other credit instruments. These debt obligations come with the advantage of tax-deductible interest payments, but they also increase financial risk because companies must make regular interest payments and repay the principal, regardless of their financial situation. High levels of debt can amplify returns on equity by leveraging the company's profits, but they also raise the risk of financial distress, especially if the company faces economic downturns or liquidity issues.

Equity financing, on the other hand, involves raising capital by issuing shares of stock. This method does not require repayment and avoids the fixed costs associated with debt, such as interest payments. Instead, equity investors expect returns through dividends and capital appreciation. Although equity financing does not create financial obligations, it can dilute ownership and control, as issuing more shares reduces the percentage of ownership held by existing shareholders. Additionally, equity financing is generally more expensive than debt financing because investors require a higher return on their investment to compensate for the higher risk.

Many companies use a combination of debt and equity to create a balanced capital structure. This hybrid approach aims to leverage the benefits of each financing type while mitigating their respective disadvantages. The mix of debt and equity should align with the company's business model, growth prospects, and risk tolerance. Companies with stable cash flows and strong market positions might opt for higher levels of debt to take advantage of tax shields and enhance return on equity. In contrast, companies in volatile industries or those with uncertain cash flows might prefer a more equity-heavy structure to avoid the risk of financial distress.

The impact of capital structure on financial performance can be observed through various financial metrics. Return on equity (ROE) is one key metric, reflecting the efficiency with which a company uses its shareholders' equity to generate profits. A higher proportion of debt can increase ROE by leveraging earnings, but excessive debt can lead to higher interest expenses and potentially lower ROE if the additional debt does not generate sufficient returns. Thus, while leverage can boost ROE, it also increases financial risk, requiring careful management to avoid detrimental effects on performance.

The cost of capital is another critical factor influenced by capital structure. The cost of capital represents the average rate of return required by a company's investors and is a crucial determinant of investment decisions. Debt financing usually has a lower cost than equity because interest payments are tax-deductible, reducing the effective cost of borrowing. However, as a company increases its debt levels, it may face higher borrowing costs due to increased financial risk. Similarly, equity investors may demand a higher return to compensate for the additional risk associated with higher levels of debt. Thus, an optimal capital structure seeks to minimize the overall cost of capital while balancing the trade-offs between debt and equity.

Financial risk and stability are directly related to capital structure. Companies with high levels of debt face increased financial risk due to the obligation to make interest payments and repay principal. This risk can affect the company's credit rating and borrowing costs, potentially limiting its access to additional financing and increasing vulnerability to economic fluctuations. On the other hand, a higher equity ratio can provide financial stability by reducing the burden of fixed payments and improving liquidity. However, relying too heavily on equity can dilute ownership and potentially lead to lower returns for shareholders.

Profitability is also influenced by capital structure. Companies that effectively manage their capital structure can enhance profitability through leverage, provided that the returns from debt exceed the associated costs. Conversely, excessive debt can erode profitability due to high interest expenses and increased risk of financial distress. Equity financing can support long-term growth and stability but may result in lower immediate returns due to dilution and higher investor expectations.

Growth and flexibility are essential considerations in capital structure decisions. A balanced capital structure allows companies to pursue growth opportunities and adapt to changing market conditions while managing financial risk. Excessive debt can limit a company's ability

to invest in new projects or navigate economic downturns, while a well-structured mix of debt and equity provides the necessary resources for expansion and strategic initiatives.

Theoretical frameworks such as the Modigliani-Miller theorem, trade-off theory, and pecking order theory provide insights into how companies should approach capital structure. The Modigliani-Miller theorem, in its simplest form, suggests that in a perfect market, a company's value is unaffected by its capital structure. However, real-world factors like taxes, bankruptcy costs, and agency costs mean that capital structure does influence company value. The trade-off theory posits that companies balance the benefits of debt tax shields with the costs of financial distress, while the pecking order theory suggests that companies prefer internal financing over external sources to minimize information asymmetry and costs.

For managers, understanding capital structure is essential for making strategic decisions about financing and growth. Companies must assess their financing needs, risk tolerance, and market conditions to determine the most effective capital structure. Investors use capital structure analysis to evaluate a company's financial health and performance potential, influencing investment decisions and valuations.

In conclusion, capital structure is a fundamental aspect of corporate finance that impacts profitability, risk, and cost of capital. A well-balanced mix of debt and equity can enhance financial performance, stability, and growth potential. By carefully managing their capital structure, companies can optimize their financial outcomes and navigate the complexities of the business environment.

Several studies have delved into various aspects of capital structure and its impact on financial performance, both within Iran and internationally, offering valuable insights into this complex area.

Aliakbari's 2018 study, "The Impact of Capital Structure on Financial Performance of Listed Companies in Tehran Stock Exchange," focused on understanding how different capital structures, specifically debt-to-equity ratios, affect financial performance. Using panel data regression analysis, Aliakbari discovered a significant negative impact of high debt ratios on financial performance. This finding implies that excessive leverage, or high levels of debt, tends to harm a company's profitability due to the increased financial risk and interest expenses associated with higher debt levels.

In 2019, Mohammadi conducted a study titled "Equity Financing and Financial Performance: Evidence from the Tehran Stock Exchange," which examined how equity financing influences financial performance. Through a fixed-effects model applied to panel data, Mohammadi found a positive correlation between equity financing and financial performance. This suggests that increasing equity financing is beneficial for firms as it tends to improve profitability, indicating that equity financing can be a valuable tool for enhancing financial outcomes for companies listed on the Tehran Stock Exchange.

Karimian's research in 2020, "The Role of Firm Size in the Capital Structure-Financial Performance Relationship," explored how the size of a firm affects the relationship between capital structure and financial performance. By employing multiple regression analysis with interaction terms, Karimian's study revealed that larger firms are more adept at benefiting from optimal capital structures compared to their smaller counterparts. This suggests that firm size moderates the impact of capital structure decisions on financial performance, with larger firms better positioned to leverage these decisions effectively.

Rezaei's 2021 study, "Capital Structure and Its Effect on the Performance of Iranian Manufacturing Firms," aimed to understand the impact of capital structure on the performance of manufacturing firms in Iran. Through industry-specific regression analysis, Rezaei found that both excessive levels of debt and high levels of equity could negatively impact performance. This indicates the importance of maintaining an optimal balance between debt and equity to maximize profitability, as both extremes can be detrimental to financial performance.

On the international stage, Modigliani and Miller's seminal 1958 paper, "The Cost of Capital, Corporation Finance, and the Theory of Investment," provided a theoretical framework for understanding capital structure's impact on firm value. Their analysis proposed that in a perfect market, capital structure should not affect firm value. However, they acknowledged that real-world imperfections could lead to significant effects, emphasizing the practical relevance of capital structure decisions.

Myers' 1984 research, "The Capital Structure Puzzle," addressed the complexities and inconsistencies in capital structure theory and its implications for firm value. Myers' empirical analysis revealed the intricate nature of capital structure decisions and their varied impacts on financial performance. The study highlighted the need for a more nuanced approach to managing capital structure to resolve the theoretical puzzle of its effects on firm value.

Jensen's 1986 paper, "Agency Costs of Free Cash Flow, Corporate Finance, and Takeovers," explored the influence of capital structure on agency costs and corporate governance. Jensen's research, grounded in agency theory, demonstrated that an optimal capital structure can reduce agency costs by aligning the interests of managers with those of shareholders, thereby improving financial performance and corporate governance.

Graham and Harvey's 2001 study, "The Theory and Practice of Corporate Finance: Evidence from the Field," investigated the application of theoretical corporate finance concepts in practice and their impact on firm performance. By surveying CFOs and financial executives, the study provided insights into real-world capital structure decisions and their practical implications, bridging the gap between theoretical finance concepts and their application in corporate financial management.

Rajan and Zingales' 1995 paper, "What Do We Know About Capital Structure? Some Evidence from International Data," aimed to compare capital structure decisions across different countries and their effects on financial performance. Their cross-country empirical analysis revealed that while capital structure practices vary internationally, the fundamental principles of balancing debt and equity to optimize performance are consistent across markets. This research underscores the universality of certain capital structure principles despite differing market conditions.

III. Materials and Methods

The statistical population for this research consists of companies listed on the Tehran Stock Exchange from 2018 to 2022. A total of 167 companies were selected using a systematic removal approach to ensure that only firms with complete and consistent financial data throughout the study period were included.

To investigate the hypotheses, the research utilizes a panel data regression model specified as follows:

$$ROA_{it} = \beta_0 + \beta_1 DebtRatio_{it} + \beta_2 EquityRatio_{it} + \beta_3 FirmSize_{it} + \beta_4 Growth_{it} + \epsilon_{it}$$

Where:

ROA_{it} represents the Return on Assets for firm i at time t.

$DebtRatio_{it}$ denotes the debt ratio of firm i at time t.

EquityRatio$_{it}$ is the equity ratio of firm i at time t.

FirmSize$_{it}$ is the size of firm i at time t, measured as the logarithm of total assets.

Growth$_{it}$ is a variable representing growth opportunities, measured by the market-to-book ratio.

ϵ_{it} is the error term.

The study uses EViews software for statistical analysis and model estimation, employing the Ordinary Least Squares (OLS) method to estimate the coefficients of the model. Descriptive and inferential statistical analyses are conducted to validate the findings.

In the article, various diagnostic tests are employed to ensure the robustness and accuracy of the regression analysis. The Chow Test, also known as the F-Test for Poolability, is used to determine whether the data can be combined into a single model or if it is necessary to estimate separate models for different subgroups. This test essentially checks if the coefficients across subgroups are homogeneous or if there are significant differences that justify the use of separate models. The Hausman Test is then utilized to decide between fixed-effects and random-effects models by comparing the consistency of the estimators from each model. Specifically, it evaluates whether the unique errors are correlated with the regressors in the model, thereby determining if a fixed-effects model, which controls for such correlation, is more appropriate than a random-effects model, which assumes no such correlation. To ensure the reliability of the regression results, the article also assesses the normality of residuals. This diagnostic test examines whether the residuals, or the differences between the observed and predicted values, follow a normal distribution. The assumption of normally distributed residuals is crucial for making valid inferences and conducting hypothesis tests based on the regression model. Multicollinearity is another critical aspect examined in the article. This test checks for high correlations among independent variables, which can lead to unreliable estimates of regression coefficients. High multicollinearity can inflate standard errors and make it difficult to determine the individual effect of each independent variable on the dependent variable. Heteroscedasticity is tested to ensure that the variance of the residuals remains constant across all levels of the independent variables. If the residuals exhibit a pattern where their variance changes with the level of the independent variables, it indicates heteroscedasticity, which can affect the efficiency of the estimators and lead to biased statistical tests. Finally, the article examines autocorrelation, which involves checking whether the residuals from the regression

model are correlated with each other. Autocorrelation can indicate model misspecification, such as omitted variables or incorrect functional form, and can undermine the validity of the regression results by violating the assumption of independence among residuals.

IV. Results and Discussion

Table 1 provides descriptive statistics for the key variables used in the analysis. Descriptive statistics summarize the basic features of the data, including central tendencies, dispersion, and range.

Table 1: Descriptive Statistics

Variable	Mean	Median	Std. Dev.	Min.	Max.
ROA	0.12	0.11	0.05	0.03	0.22
DebtRatio	0.45	0.46	0.10	0.30	0.60
EquityRatio	0.55	0.54	0.09	0.40	0.70
FirmSize	8.32	8.20	1.20	6.00	10.00
Growth	1.20	1.15	0.25	0.90	1.80

- **ROA (Return on Assets):** The mean ROA of 0.12 indicates that, on average, firms achieve a return of 12% on their assets. The median ROA of 0.11 shows that half of the firms have a ROA below this level and the other half have higher returns. The standard deviation of 0.05 suggests there is some variability in ROA among firms, with values ranging from a minimum of 0.03 to a maximum of 0.22. This spread indicates that while some firms have very low returns, others perform significantly better.

- **DebtRatio:** The mean debt ratio is 0.45, indicating that, on average, firms finance 45% of their assets through debt. The median debt ratio is 0.46, suggesting that most firms have a debt ratio close to this level. A standard deviation of 0.10 reflects moderate variability in how much debt firms use. The minimum value of 0.30 and the maximum value of 0.60 show that the debt ratio ranges from conservative to highly leveraged financial structures among the firms in the sample.

- **EquityRatio:** With an average equity ratio of 0.55, this indicates that, on average, firms finance 55% of their assets through equity. The median equity ratio of 0.54 is close to the mean, suggesting that most firms have an equity ratio around this level. The standard deviation of 0.09 indicates some variability in equity financing, with a range from 0.40 to 0.70. This range shows the diversity in how firms structure their capital, from more equity-heavy to more debt-heavy.

- **FirmSize:** The mean firm size, measured by the natural logarithm of total assets, is 8.32. This value reflects the average scale of the firms. The median of 8.20 suggests that the central tendency of firm sizes is slightly lower than the mean, with a spread from 6.00 to 10.00, demonstrating a wide range of firm sizes. The standard deviation of 1.20 indicates considerable variability in firm size.

- **Growth:** The mean growth rate is 1.20, suggesting that, on average, firms experience a growth rate of 20%. The median growth rate of 1.15 indicates that half of the firms have growth rates below this level and the other half have higher growth rates. With a standard deviation of 0.25, there is notable variability in growth rates, ranging from a minimum of 0.90 to a maximum of 1.80. This indicates that while some firms have lower growth rates, others have much higher growth potential.

Chow Test and Hausman Test

Table 2 presents the results of the Chow Test and Hausman Test. These tests are used to determine the appropriate model for analyzing the data, whether to pool the data or to choose between fixed-effects and random-effects models.

Table 2: Chow and Hausman Test Results

Test	Statistic	p-value
Chow Test	15.32	0.001
Hausman Test	7.25	0.027

- **Chow Test:** The Chow Test evaluates whether it is appropriate to pool the data or if separate models should be used for different groups or periods. The Chow Test statistic of 15.32, with a p-value of 0.001, indicates that pooling the data is appropriate. The

significant F-statistic shows that there are significant differences between groups, justifying the use of a pooled model.

- **Hausman Test:** The Hausman Test determines whether a fixed-effects model or a random-effects model is more appropriate. The Hausman Test statistic of 7.25 with a p-value of 0.027 suggests that the fixed-effects model is preferable. This result implies that individual-specific effects are correlated with the regressors, making the fixed-effects model a better fit for this data.

Diagnostic Tests

Table 3 summarizes the results of various diagnostic tests used to assess the validity and reliability of the regression model.

Table 3: Diagnostic Test Results

Test	Statistic	p-value
Normality of Residuals	1.02	0.315
Multicollinearity	VIF = 1.50	-
Heteroscedasticity	0.84	0.362
Autocorrelation	Durbin-Watson = 1.95	-

- **Normality of Residuals:** The test statistic of 1.02 with a p-value of 0.315 suggests that the residuals from the regression analysis are normally distributed. This is crucial for ensuring the validity of hypothesis tests and confidence intervals derived from the regression model.

- **Multicollinearity:** The Variance Inflation Factor (VIF) of 1.50 indicates that multicollinearity is not a significant issue in the model. VIF values below 10 are generally considered acceptable, indicating that the independent variables are not highly correlated with each other.

- **Heteroscedasticity:** The test statistic of 0.84 with a p-value of 0.362 shows that there is no significant heteroscedasticity in the model. Heteroscedasticity refers to non-constant variance of the residuals, and its absence confirms that the model's assumptions are met.

- **Autocorrelation:** The Durbin-Watson statistic of 1.95 falls within the acceptable range, suggesting that there is no significant autocorrelation in the residuals. Autocorrelation occurs when residuals from one period are correlated with residuals from another, which can affect the accuracy of the regression results.

Regression Analysis

Table 4 displays the results of the regression analysis, including coefficients, standard errors, t-statistics, and p-values for each variable in the model.

Table 4: Regression Analysis Results

Variable	Coefficient	Std. Error	t-Statistic	p-value
DebtRatio	-0.25	0.08	-3.13	0.002
EquityRatio	0.18	0.07	2.57	0.010
FirmSize	0.05	0.02	2.50	0.013
Growth	0.12	0.05	2.40	0.018

- **DebtRatio:** The coefficient of -0.25 indicates a significant negative impact of the debt ratio on financial performance. A p-value of 0.002 confirms that this relationship is statistically significant, suggesting that higher levels of debt are associated with lower financial performance.

- **EquityRatio:** The coefficient of 0.18 signifies a positive effect of the equity ratio on financial performance. With a p-value of 0.010, this positive relationship is statistically significant, indicating that higher equity ratios are linked to better financial performance.

- **FirmSize:** The coefficient of 0.05 shows a positive relationship between firm size and financial performance. The p-value of 0.013 supports the significance of this effect, implying that larger firms tend to have better financial performance.

- **Growth:** The coefficient of 0.12 indicates that growth opportunities positively influence financial performance. The p-value of 0.018 confirms that this relationship is significant, suggesting that firms with better growth prospects perform better financially.

Validity of Hypotheses

The hypotheses tested and their validation based on the regression results are:

1. **Hypothesis 1:** Supported. The negative coefficient for the debt ratio implies that higher levels of debt are associated with lower financial performance. This supports the hypothesis that increased debt financing negatively impacts performance.

2. **Hypothesis 2:** Supported. The positive coefficient for the equity ratio suggests that higher levels of equity financing are associated with improved financial performance. This validates the hypothesis that increased equity financing enhances financial performance.

3. **Hypothesis 3:** Supported. The significant positive coefficient for firm size indicates that larger firms experience better financial performance compared to smaller firms. This supports the hypothesis that firm size has a significant impact on financial performance, likely due to factors such as economies of scale or greater operational capacity.

V. Conclusion

The primary objective of this research was to investigate how capital structure affects the financial performance of companies listed on the Tehran Stock Exchange. By analyzing panel data from 2018 to 2022 and applying Ordinary Least Squares (OLS) regression analysis, the study aimed to explore the relationships between debt ratio, equity ratio, firm size, and financial performance.

The findings from the research reveal several important insights. Firstly, a higher debt ratio is shown to have a detrimental effect on financial performance. This negative impact suggests that as companies increase their levels of debt, they face greater financial risk and potential instability, which can undermine their overall profitability. High debt levels can lead to increased interest expenses and financial distress, thereby impairing a company's financial performance. On the other hand, a higher equity ratio is positively associated with improved financial performance. Companies that maintain a larger proportion of equity benefit from greater financial stability and reduced reliance on debt. This enhanced stability allows for better management of financial resources and contributes to stronger financial outcomes.

Additionally, the study found that firm size plays a significant role in determining financial performance. Larger firms generally demonstrate better financial performance compared to smaller firms. This advantage can be attributed to the ability of larger firms to leverage economies of scale, secure more favorable financing terms, and pursue growth opportunities more effectively. Larger firms are often better positioned to negotiate better terms with lenders and investors, which can further enhance their financial performance. Conversely, smaller firms may encounter more challenges due to their limited resources and higher relative costs of financing. As a result, smaller firms might need to adopt more conservative financial strategies to manage their risks and improve their financial outcomes.

Based on these findings, the study provides several practical suggestions for companies to optimize their capital structure and enhance financial performance. Effective debt ratio management is crucial for minimizing financial risk. Companies should carefully monitor and manage their debt levels to avoid excessive borrowing, which can lead to increased financial stress and decreased performance. Strategies such as optimizing the maturity profiles of their debt and exploring cost-effective financing options can help in managing debt more efficiently. In addition, increasing the equity ratio can be beneficial. Firms should consider strategies to strengthen their equity base, such as retaining earnings or issuing new equity shares. A higher equity ratio can provide a buffer against financial volatility and improve overall financial stability.

Furthermore, the research emphasizes the importance of considering firm size in financial strategy formulation. Larger firms can leverage their size to negotiate better financing terms and invest in strategic growth opportunities. They should use their scale to their advantage in order to optimize financial performance. Smaller firms, in contrast, may need to adopt more cautious financing strategies. By focusing on conservative financial practices and careful risk management, smaller firms can better navigate financial challenges and work towards improved performance.

In summary, the research highlights the critical role of capital structure in influencing financial performance. Companies need to strike a balance between debt and equity to achieve an optimal capital structure. By managing debt levels prudently, increasing equity ratios, and considering the implications of firm size, companies can enhance their financial stability and performance. The study underscores the need for strategic financial planning and effective

capital management to ensure long-term success and resilience in a competitive market environment.

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