

IMPACT OF CAPITAL STRUCTURE ON PROFITABILITY OF MANUFACTURING COMPANIES IN NEPAL

A Dissertation submitted to the Office of the Dean, Faculty of Management in partial fulfillment of the requirements for the Master's Degree

by

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CERTIFICATION OF AUTHORSHIP

I hereby corroborate that I have researched and submitted the final draft of dissertation entitled **“Impact of Capital Structure on Profitability of Manufacturing Companies in Nepal”**. The work of this dissertation has not been submitted previously for the purpose of conferral of any degrees nor it has been proposed and presented as part of requirements for any other academic purposes.

The assistance and cooperation that I have received during this research work has been acknowledged. In addition, I declare that all information sources and literature used are cited in the reference section of the dissertation.

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REPORT OF RESEARCH COMMITTEE

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This study entitled **“Impact of Capital Structure on Profitability of Manufacturing Companies in Nepal”** has been prepared in partial fulfillment for the Degree of Master of Business Studies (MBS) under the Faculty of Management, Tribhuvan University is based on research models involving the use of quantitative aspect of effect of capital structure on profitability of manufacturing companies in Nepal.

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Peshal Dhakal

Date:

TABLE OF CONTENTS

	Page No.
<i>Title Page</i>	<i>i</i>
<i>Certification of Authorship</i>	<i>ii</i>
<i>Report of Research Committee</i>	<i>iii</i>
<i>Approval Sheet</i>	<i>iv</i>
<i>Acknowledgements</i>	<i>v</i>
<i>Table of Contents</i>	<i>vi</i>
<i>List of Tables</i>	<i>viii</i>
<i>List of Figures</i>	<i>ix</i>
<i>Abbreviations</i>	<i>x</i>
<i>Abstract</i>	<i>xi</i>
CHAPTER I INTRODUCTION	1
1.1 Background of the Study	1
1.2 Problem Statement	4
1.3 Objectives of the Study	6
1.4 Hypothesis of the Study	6
1.5 Rational of the Study	6
1.6 Limitations of the Study	7
CHAPTER- II LITERATURE REVIEW	8
2.1 Theoretical Review	8
2.1.1 Theories of Capital Structure.....	8
2.1.1.1 Modigliani and Miller (MM) Theory	8
2.1.1.2 Trade-Off Theory	9
2.1.1.3 Agency Cost Theory.....	9
2.1.1.4 Pecking Order Theory	10
2.1.2 Concept of Capital Structure	11
2.1.3 Determinants of Capital Structure Decision	14
2.1.4 Company Profitability	18
2.2 Empirical Review	19
2.3 Research Gap.....	30

CHAPTER – III RESEARCH METHODOLOGY	31
3.1 Research Design	31
3.2 Population and Sample, and Sampling Design	31
3.3 Nature and Sources of Data, and the Instruments of Data Collection.....	32
3.4 Method of Analysis	32
3.5 Research Framework and Definition of Variables.....	34
CHAPTER – IV RESULTS AND DISCUSION	37
4.1 Results	37
4.1.1 Position and Status of Variables	37
4.1.1.1 Debt to Equity	37
4.1.1.2 Debt to Assets Ratio	38
4.1.1.3 Size of the Companies	39
4.1.1.4 Return on Assets.....	40
4.1.1.5 Return on Equity	41
4.1.2 Descriptive Statistics of Variables.....	42
4.1.3 Correlation Analysis	43
4.1.4 Regression Analysis	44
4.1.4.1 Analysis of Return on Assets Regression.....	44
4.1.4.2 Analysis of Return on Equity Regression	47
4.2 Discussion	49
CHAPTER – V SUMMARY AND CONCLUSION	51
5.1 Summary	51
5.2 Conclusion.....	52
5.3 Implications.....	53

References

Appendices

LIST OF TABLES

	Page No.
Table 1 Summary of Empirical Review.....	26
Table 2 Debt to Equity	38
Table 3 Debt to Assets	39
Table 4 Size of the Companies	40
Table 5 Return on Assets	41
Table 6 Return on Equity	42
Table 7 Descriptive Statistics of Variable of Manufacturing Companies	43
Table 8 Pearson Correlation Coefficients of Study Variables	44
Table 9 Model Summary	45
Table 10 Analysis of Variance (ANOVA).....	45
Table 11 Regression Coefficient of Independent Variables with ROA.....	46
Table 12 Model Summary	47
Table 13 Analysis of Variance (ANOVA).....	47
Table 14 Regression Coefficient of Independent Variables with ROE	48

LIST OF FIGURES

	Page No.
Figure 1 Research Framework of the Study	34

ABBREVIATIONS

CV	:	Coefficient of Variation
DAR	:	Debt to Assets Ratio
DER	:	Debt to Equity Ratio
DNL	:	Dabur Nepal Limited
GDP	:	Gross Domestic Products
HDL	:	Himalayan Distillery Limited
LSIZE	:	Natural Logarithm of Size or Total Assets
Ltd.	:	Limited
ROA	:	Return on Assets
ROE	:	Return on Assets
SCP	:	Structure Conduct Performance
SD	:	Standard Deviation
TU	:	Tribhuvan University
UNL	:	Unilever Nepal Limited

ABSTRACT

This study investigates effect capital structure on profitability of manufacturing companies in Nepal. Secondary data was gathered from manufacturing companies of Nepal for ten year periods (2013/14-2022/23). This study used correlation and multiple regression analysis to analyze the data. The correlation analysis shows that debt to equity ratio (DER) and debt to total assets have significant negative relation with profitability (ROA and ROE) of manufacturing companies in Nepal. Moreover, size of companies has significant negative relationship with profitability (ROA and ROE) of the manufacturing companies. The regression result reveals that debt to equity ratio has insignificant negative effect on ROA but it has significant negative impact on ROE of the manufacturing companies while debt to assets ratio has insignificant positive impact on profitability (ROA and ROE) of manufacturing companies. Further, size of companies has significant negative impact on profitability (ROA and ROE) of the manufacturing companies in Nepal. Hence, this study concluded that capital structure has insignificant impact on profitability of manufacturing companies in Nepal

Keywords: Return on assets, return on equity, debt to equity ratio, debt to assets ratio and size of companies.

CHAPTER I INTRODUCTION

1.1 Background of the Study

A company's capital structure shows how much of its capital is made up of debt. As it directly affects the company's capacity to serve the interests of its stakeholders, this ratio is significant from a financial standpoint. In order to properly manage risk and shareholder return, the decision between debt and equity financing affects the company's entire financing strategy and calls for careful balancing. A sensible balance between debt and equity helps optimize capital structure, which can increase shareholder wealth in the long run. A manufacturing company's management must make a crucial choice about the capital structure in order to maximize profitability, minimize capital expenditures, and boost shareholder value. The majority of organizations have a capital structure that combines loan and equity. The worth of the company and its strategic importance should be taken into consideration when determining how much of these two types of funding to use (Thapa et al., 2021).

The ratio of debt to equity that a company utilizes to fund its operations is known as its capital structure. A company's capital structure is made up of a variety of securities. A company's capital structure describes how it finances its activities. It can use debt, equity, or a combination of the two (Brigham & Gapenski, 2004). The percentage of debt and equity on a company's balance sheet is referred to as capital. Business enterprises typically find it challenging to determine the ideal debt to equity ratio. A company has a variety of options for capital structures. It has the option of issuing either a lot of debt or not at all. It can execute forward contracts, utilize warrants, issue convertible bonds, arrange leasing finance, and trade bond swaps. It can issue a wide range of different securities in an infinite number of combinations, but it looks for the one that will maximize its total market value (Brigham & Gapenski, 2004).

The following theories can be used to analyze a firm's capital structure decision: trade-off theory, pecking order theory, and Modigliani-Miller theory. The capital structure irrelevance proposition proposed by Modigliani and Miller in 1958 serves as

the foundation for contemporary company finance theory. There was no widely accepted theory of capital structure prior to them. When Modigliani and Miller (1958) published their well-known arbitrage argument demonstrating that a firm's market value is independent of its capital structure, the discussion surrounding how and why businesses chose their capital structure got underway. In order to begin their hypothesis, Modigliani and Miller assume that the company has a specific set of anticipated cash flows. The company must allocate the cash flows among investors after deciding on a specific ratio of debt to equity to fund its assets. Because it is believed that businesses and investors have equal access to the financial system, homegrown leverage is permitted. Therefore, the firm's market value is unaffected by its level of leverage.

The process via which a company raises money to launch and grow its commercial operations is outlined in its capital structure. It is a combination of several kinds of debt and equity capital that a company keeps as a result of its financing choices. Finance is a necessary component of all corporate activities. Businesses could not function without funding to support their fixed assets and working capital needs. The capital structure decision is the most important one when it comes to capital investment decisions since it has a direct impact on an enterprise's profitability. As such, careful consideration must be paid while choosing a capital structure (Bhattarai, 2005).

The company's two primary decision-making domains are funding and investing. The capital structure decision-making process is the method by which the business is financed by a combination of debt and equity. The directors are interested in selecting the ideal capital structure for their company while making funding decisions for the company. Choosing how much leverage to use is another crucial decision that the administration of the organization makes. The concepts of capitalization, leverage ratio, capital structure, and financial structure are all the same and are connected to the types of sources and sums of money that the company has employed to build them and purchase assets (Barges, 2009).

One of the most crucial decisions a financial manager makes is the choice of capital structure. The reason for this is that the ideal capital structure reduces the total cost of

capital while maximizing shareholder wealth. Understanding the financial structure is necessary before understanding the capital structure (Gautam & Thapa, 2004).

A company's capital structure, often known as its capitalization, is its long-term debt, preferred stock, and shareholder equity. The capital structure of a company is therefore merely its financial structure. The capital structure of a company has a role in determining its level of liquidity as well as its potential to achieve long-term profitability. Only long-term debt and the entire investment made by stockholders are included in the term. Some businesses don't design their capital structure; instead, it emerges organically from the finance manager's judgment call without any official preparation. These businesses might succeed in the near term, but in the long run, they might have a lot of trouble raising money to support their operations. Unplanned capital structures can also prevent these businesses from using their money as efficiently as possible. The finance manager need to, in theory, design his company's ideal capital structure. When the market value per share reaches its maximum, the ideal capital structure is achieved. Determining the ideal capital structure in practice is a difficult task that requires thinking beyond the box (Barges, 2009).

Sharma (2019) discovered that the capital structure, which is the ratio of total debt to total assets at book value, affects the firm's riskiness and profitability. According to the definitions provided by numerous earlier scholars, capital structure is the mix of debt and equity used to finance a corporate entity. Equity is created when businesses sell a portion of their ownership stake in order to raise money for operations and capital projects. A contractual arrangement known as debt requires businesses to borrow money and return it with interest within a predetermined period of time. A united capital structure will prevent most businesses from using their assets as efficiently as possible. Because capital structure has a direct bearing on a company's performance, choosing the right debt to equity ratio is still crucial.

The most important choice a manufacturing company's management makes to optimize profitability and reduce capital expenses and ultimately maximize stockholder wealth is the capital structure decision. There are essentially two main sources of funding. Debt makes up external finance, whilst equity makes up internal funding. Most businesses have a capital structure that consists of both debt and equity.

Modigliani and Miller (1963) defined capital structure as the mix of debt and equity that a business utilizes to run. They also shown how capital structure and corporate performance are related. Shrestha (2023) addressed about the connection between profitability and capital structure.

Profitability ratios are essential for assessing a company's financial performance. Efficiency is measured by profitability, which in turn determines the success or failure of an endeavor. A prudent combination or mix of debt to equity is crucial for financial organizations to optimize profit. Therefore, the purpose of this study was to investigate how capital structure affects the profitability of Nepalese manufacturing enterprises, with a focus on the profitability of core business operations. This will give financial managers practical understanding of potential issues with capital structure and profitability, as well as help them determine the ideal level of capital structure to reach the highest possible level of company profitability and, consequently, maximize shareholder wealth.

1.2 Problem Statement

Significant challenges are currently facing Nepalese industrial sector, as numerous companies are closing or are about to close. The industry has low profit margins even with its potential for profitability. For Nepalese manufacturing industry to thrive, access to raw materials and the availability of competent labor are essential. Considering Nepal's impoverished state, industrial growth raises the level of living for its people. However, little study has been done, so it is unknown how manufacturing companies are currently doing, and there are a number of difficulties that need to be addressed in order to improve corporate performance.

Ramadan and Ramadan (2015) revealed that the long-term debt to capital ratio, total debt to capital ratio and total debt to total assets ratio had statistically significant adverse relationship with performance and capital structure. Revathy and Santhi (2016) found that there was a direct correlation between capital structure variables and profitability and debt-to-equity ratio had a negative impact on manufacturing companies' profits.

Olusuyi and Felix (2017) concluded that the debt-to-equity ratio had a statistically significant negative impact on financial performance. Kalyani and Mathur (2018) found that log sales, the degree of operating leverage, and the growth of the asset were significant variables in determining profitability. Dhodary (2019) concluded that asset tangibility, profitability, liquidity, and interest coverage ratio are the major factors of profitability. Jaishi and Poudel (2019) found leverage was significantly influenced by size, tangibility, profitability, and growth. Mouna et al. (2019) found that size had significant positive impact on performance and that the debt-to-equity ratio had a negative and significant impact on profitability.

Rahman et al. (2019) stated that the debt to equity ratio significantly impacted ROA negatively, but the debt ratio and equity ratio significantly impacted ROA positively. Ayange et al. (2021) showed that Nigerian businesses are heavily dependent on short-term debt financing, which lends credence to the pecking order theory. Ngoc et al. (2022) examined that debt to assets significantly reduced ROA. However, ROA was significantly improved by tangibility and liquidity. Huong (2023) discovered that the profitability of businesses is significantly impacted by both the short- and long-term debt ratios. Shrestha (2023) found that return on equity was not significantly impacted by the debt to equity, debt to assets, or equity to total assets ratios. However, there aren't many studies in the specific field of manufacturing companies, thus this study fills a need in the sector. The study's goal was to investigate how capital structure affects the profitability of Nepalese manufacturing businesses. More specifically this study seeks to solve the answer of following question:

- What is the position of capital structure and profitability of manufacturing companies in Nepal?
- What is the relationship between capital structure variables such as debt to equity ratio, debt to assets ratio and size of companies and profitability of manufacturing companies in Nepal?
- What is the impact of debt to equity ratio, debt to assets ratio and size of companies on profitability of manufacturing companies in Nepal?

1.3 Objectives of the Study

The main purpose of this study is to examine the impact of capital structure on profitability in manufacturing companies in Nepal. The other specific objectives are as follows:

- To analyze the position of capital structure and profitability of manufacturing companies in Nepal.
- To examine the relationship between capital structure variables such as debt to equity ratio, debt to assets ratio and size of companies and profitability of manufacturing companies in Nepal.
- To assess the impact of debt to equity ratio, debt to assets ratio and size of companies on profitability of manufacturing companies in Nepal.

1.4 Hypothesis of the Study

The researcher expected with better capital structure management with high return on asset (ROA). With the help of data the study was established and tested the following hypothesis:

Hypothesis 1 (H_1): There is significant impact of debt to equity ratio on the profitability of manufacturing companies in Nepal.

Hypothesis 2 (H_1): There is significant impact of debt to assets ratio on the profitability of manufacturing companies in Nepal.

Hypothesis 3 (H_1): There is significant impact of size of companies on the profitability of manufacturing companies in Nepal.

1.5 Rational of the Study

Nepal's manufacturing industry is growing every day. The country has been dealing with several challenges lately, and as a result, the manufacturing sector is operating slowly. In this case, the study will help the companies manage their capital structure overview and develop future strategies to perform significantly better in the long run. This study will benefit all companies in the population, not just the ones that were sampled. Additionally, this study may aid concerned academics, professionals, investors, and scholars. Additionally, this study will assist in educating decision-makers on the value of capital structure management for their continued success.

Research and studies on capital structure and its impact on a company's performance, particularly in the context of manufacturing firms, are scarce in Nepal. Decisions about the application, investment, and hiring of the company's capital fund are crucial for the financial managers to make since they impact the capital structure of the business. One of the most crucial elements of a business is its capital structure, which has a long-term impact on both the profitability and sustainability of the enterprise.

The research's conclusions and suggestions assist investors in making wise financial choices. It also supports the financial management in making critical strategic choices about the company's debt-to-equity ratio. From an academic standpoint, it adds value for the researchers because it provides a foundation for future studies on capital structures and how they affect the manufacturing industries' profitability.

The findings of this study give managers, business advisors, and investors the financial know-how they need to combine debt and equity and optimize corporate success.

1.6 Limitations of the Study

The limitations of the study are as follows;

- This study only focus impact of capital structure on profitability of three manufacturing companies which are Unilever Nepal Limited, Dabur Nepal Private Limited and Himalayan Distillery Limited.
- The study covers only the latest ten fiscal years i.e. 2013/14 to 2022/23.
- The study is based on secondary data such as book, journals, articles and audited financial report of respective manufacturing companies.
- This study is used descriptive statistic, correlation analysis and multiple regression analysis to analyze the data.

CHAPTER- II

LITERATURE REVIEW

A crucial and essential step in any research project is the review of the literature. It entails going over research papers or other pertinent claims in the relevant field of study in order to become aware of all previous studies, their shortcomings, and their findings so that new research can be carried out. This chapter looks at and reviews a few books, articles, published and unpublished articles in various economic journals, magazines, newspapers, and the annual balance sheet of the relevant banks on connected topics. It also conducts a subject-related web search. For this reason, this chapter is split into two sections: an empirical review and a theoretical review.

2.1 Theoretical Review

2.1.1 Theories of Capital Structure

This study reviews the following theories: peaking order theory, trade-off theory, agency cost theory, and Modigliani and Miller (MM) theory.

2.1.1.1 Modigliani and Miller (MM) Theory

The groundbreaking research on capital structure done by Modigliani and Miller in 1958 served as a foundation for the construction of the theoretical framework that would eventually house a number of different ideas related to corporate finance. The well-known idea of "capital structure Irrelevance," which holds that financial leverage has no bearing on a firm's value, was reached by Modigliani and Miller in 1958. Their hypothesis, however, was predicated on extremely narrow premises that are untrue in practice. These presumptions include ideal capital markets, homogeneous expectations, no taxes, and no transaction costs. The concept of a "optimal" capital structure, which optimizes the firm's worth and hence lowers its overall cost of capital, is brought about by the existence of bankruptcy costs and tax advantages associated with interest payments.

In 1958, Modigliani and Miller reexamined their previous stance by including tax benefits as factors influencing a firm's capital structure. The fact that interest is a tax-deductible expense is the main characteristic of taxes. A company that pays taxes gets

a "tax-shield" in the form of decreased taxes paid, which partially offsets the interest. Therefore, Modigliani and Miller (1963) suggested using as much loan capital as possible to boost profitability and thereby optimize enterprises' value.

2.1.1.2 Trade-Off Theory

According to the trade-off theory of capital structure, a business weighs the costs and advantages of using different levels of debt and equity financing to choose how much of each to employ. The traditional version of the theory took into account striking a balance between the tax benefits of debt and the deadweight costs of bankruptcy. It claims that there are costs associated with financing with debt, such as the expenses of financial difficulty, as well as benefits associated with debt, such as tax advantages (Kraus & Litzenberger, 1973).

Anticipated expenses linked to financial difficulties significantly reduce a company's worth, acting as a counterbalance to the tax benefits of taking on more debt. Conversely, there is a claim that capital is extremely expensive. In order to offset the higher bankruptcy risk linked to the likelihood of financial difficulties and a correspondingly low capital ratio, investors seek a premium. Commercial banks must take on greater risk in order to earn a larger risk premium on their investments in order to produce a "adequate" return on equity. This risk premium increases as capital levels rise. Therefore, in order to avoid an inefficient cost of capital, more risk calls for higher percentages of equity in the company's capital structure. It is unclear what the buffer effect and this negative incentive effect will ultimately result in. It's feasible that when capital levels rise, the default risk will rise as well (Brealey & Myers, 2003).

2.1.1.3 Agency Cost Theory

According to agency theory, a firm is a "nexus of contracts" made up of several resource providers. The two main players in agency theory are agents, who run the day-to-day operations of the company, and principals, who provide funding. The organization incurs agency costs because the agents' interests aren't always the principal's. These costs include the cost of keeping an eye on agents' behavior, which includes budgetary constraints, pay policies (such as stock options, bonuses, and other

incentives), and the loss of earnings as a result of operating regulations and management limits.

The expenses of sub-optimal decisions—described as choices that are made with the interests of agents rather than principals—as well as the bonding costs of the agents are also included. According to agency theory, managerial decisions in the modern firm, whose share ownership is widely held, deviate from those necessary to maximize returns to shareholders (Berle & means 1932; Pratt & Zeckhauser, 1985). Agency theory outlines ways to minimize agency loss, such as manager incentive programs that pay them for maximizing the interests of shareholders.

2.1.1.4 Pecking Order Theory

Myers and Majluf (1984) introduced the pecking order hypothesis, which is predicated on the idea of asymmetric information. It makes the case that managers are more knowledgeable than outside investors about the potential, dangers, and worth of their organization. In this instance, management's selection of a capital source that accords greater weight to sources that disclose the least amount of information influences the capital structure decision. The decision to issue debt or stock and to choose between internal and external finance is thus influenced by asymmetric information. When management decides to issue fresh shares to fund a new project, external investors may see this as a signal that the company is overpriced, which could lead to a decline in the share price and a reduction in the firm's value (Brigham & Erhardt, 2005). Conversely, fresh debt is seen as a positive indication of the company's future potential.

According to the theory, there is a hierarchy or sequence for financing new initiatives. Businesses would rather employ retained earnings, or internal finance, first and external funding second. Retained earnings don't come with flotation fees and don't need outside oversight from the capital source. This theory, which takes a behavioral approach to capital structure, is predicated on the idea that finance decisions are made in a way that makes management's job easier and less complex. It is common for managers to take the path of least resistance and finance their operations at the lowest possible cost. Pecking order theory predicts that highly profitable organizations will be less leveraged than less profitable firms because they will have more internal funds

available as retained earnings to finance their deficits (Shyam-Sunder & Myers, 1999). A company that requires outside funding will turn to debt rather than stock since debt is thought to be less expensive than equity. As a result, changes in a company's debt ratio are determined by its requirement for outside funding rather than by its desire to achieve the ideal capital structure.

2.1.2 Concept of Capital Structure

Capital is a synonym for funds or money. Without money, nobody takes any action. The capital possesses both return and risk characteristics. Therefore, to achieve a high return at a manageable level of risk, the ideal capital combination is needed. This ideal capital mix is managed through a process known as capital structure management. Debentures, long-term debt, preference shares, equity shares, and short-term debt—which also includes retained earnings, reserves, and surplus—are the sources of capital. Every kind of fund carries some risk. Their required rates of return vary. Compared to debt, common stock has a higher risk and requires a higher rate of return. As a result, the company must build a portfolio of these kinds of assets, which have a lower cost of capital and a larger return. Additionally, the company must produce at least enough cash flow to cover its debt holders, preference shareholders, and investors. Therefore, in order to maximize shareholder wealth, the company should generate more cash flow than only meet investor expectations. It should also work to acquire the necessary capital as quickly and cheaply as feasible (Gautam & Thapa, 2004).

A group of products and money that can be used to generate income in the future is referred to as capital. Consumer items and money spent on pleasure and immediate need are typically excluded from the definition and economic theory of capital. Therefore, a firm considers its accessible stocks, bonds, bank balances, land, buildings, machinery, inventory, and raw materials to be its capital. Goods purchased for personal use, such as homes, furniture, vehicles, and other items, are not traditionally regarded as capital (Barges, 2009).

Different academics and professionals use different terms when referring to capital. Wealth is defined by economists as net assets or stockholders' interest as indicated by

the balance sheet or the net worth of shareholders' equity; businesspeople refer to wealth as total assets. A lawyer would refer to it as capital stock. Capital, whatever term is chosen, is the money produced to finance various assets, whether they are long-term or short-term. As a result, capital is a combination of short- and long-term finances (Bhattarai, 2005).

Since a variety of factors affect a company's decision regarding its capital structure, there is significant variance in capital structure across industries and even across individual companies within any given industry. A key factor is the decision-maker's judgment when it comes to capital structure. These are qualitative and highly psychologically complex aspects that don't always follow conventional wisdom because financial markets aren't flawless and decisions must be made with imperfect information and risk (Francis, 2002).

The goal of profit maximization depends on capital structure planning, which guarantees the lowest possible cost of capital and the highest possible rate of return to equity holders. The types of capital that make up a company's financial basis, or its capital mix, are just as significant as the quantity of capital required by the organization. How much of the equity money will be used to represent the investors' funds in the businesses? The ratio of debt to equity securities that would optimize stock value is determined by a financial manager. An ideal capital structure is needed in order to reduce the opportunity cost of capital and maximize shareholder wealth. Debt is a crucial component of capital structure since it establishes the leverage company. When a company has a high operational income, it boosts shareholder returns; nevertheless, when the company has a low operating income, it worsens shareholder returns (Gautam & Thapa, 2004).

Capital structure refers to the combination of several securities held by the company. Choosing a capital structure is essentially a marketing decision. The company can issue dozens of different securities in an infinite number of combinations, but it looks for the one that will maximize its total market worth. Both current and fixed assets are financed through several sources. Although the sources of funding can be both short- and long-term, they are often divided into debt and equity, which define the capital structure of the company (Pradhan, 2003).

Typically, financial and capital structure are distinguished. All sources, both short- and long-term, used to finance all of a company's assets are referred to as its financial structure. However, the capitalization portion of a firm's total is considered its capital structure, which solely consists of long-term resources like stock and debt as a result, the financial structure includes the capital structure. The capital structure composition varies throughout companies and is subject to direct guidance and control by the management. However, by taking into account pertinent factors and examining how alternative financing plans affect earnings per share, an acceptable and satisfactory capital structure can be established (Chandra, 1985).

Long-term debt and equity are combined to form the capital structure. It is a component of equity, long-term debt, and financial stock. The whole combination of preferred stock, common stock, long-term debt, and current obligations makes up this component of the financial structure. We obtain the capital structure when we subtract current obligations from it (Mathur, 1997).

The combination of debt and equity that will optimize the company's market value is known as the optimal capital structure. If there is an optimal state, it has two aspects. First off, it increases the company's worth and, consequently, the owners' wealth. It also lowers the company's cost of capital, which makes it easier for it to identify new investment opportunities that can generate wealth. The permanent financing of the company is reflected by its capital structure, which is mostly made up of long-term debt, preferred stock, common stock, capital surplus, and cumulative retained earnings. Similar to cost of capital and, thus, capital budgeting decision, leverage and capital structure are closely related concepts. Leverage is the outcome of using fixed-cost assets to increase the owners' return on investment for the company. Leverage changes impact the level of return and related risk. Leverage typically translates into higher risk and returns. The degree of leverage in a company's capital structure, as well as the proportion of long-term debt and equity that the company maintains, can have a big impact on its value by influencing risk and return. When trying to design the optimal capital structure, the finance team needs to be aware of how to monitor and assess leverage due to its impact on value (Gitman, 2001).

Expected profit margin is often increased by financial leverage; nevertheless, as the debt-to-assets ratio rises, so does the interest rate on debt and the needed rate of return on equity. Leverage therefore has two opposing effects: it raises EPS, which raises stock price, but it also increases risk, which lowers stock price. Nonetheless, there is a debt-to-assets ratio that achieves the best possible balance between these conflicting consequences. This ratio, which optimizes the price of the company's stock, is known as the optimal capital structure (Weston & Brigham, 1995).

2.1.3 Determinants of Capital Structure Decision

Capital structure is the combination of long-term funding sources that optimizes the value of the company and its stockholders. The primary idea of an ideal capital structure is provided by the concept and definition of capital structure. The finance manager need to, in theory, design his company's ideal capital structure. When the market value per share reaches its maximum, the ideal capital structure is achieved. When the marginal costs of all the funding sources are equal, the values will be maximized. Finding the ideal capital structure is a difficult undertaking that requires using more than just theory in real-world situations. In terms of capital structure, industries and individual enterprises within an industry differ significantly from one another. The judgment of the individual making the capital structure choice is vital since many factors affect a company's capital structure decision (Weston & Brigham, 1995).

Asset structure

The company that uses debt extensively is usually one whose assets make good collateral for loans. Therefore, manufacturing firms that heavily invest in specialized machinery and work-in-progress tend to utilize less debt than real estate companies, which tend to be highly leveraged.

Operating leverage

If everything else stays the same, a company with lower operating costs can use financial leverage more effectively since operational and financial leverage work together to determine how much a company's sales will fall overall in terms of operating income and net cash flows.

Sale stability

Compared to a company with erratic revenues, one with generally constant sales may afford to pay greater fixed charges and take on more debt. Because of their consistent demand, utility companies have generally been able to use more financial leverage than industrial corporations (Gautam & Thapa, 2004).

Profitability

It's well known that companies with extremely high rates of return on investment employ comparatively low levels of debt. Although there is a theoretical explanation for this, it appears that very successful companies like IBM and KODAK can get by without doing much debt financing. They are able to finance the majority of their operations mostly from retained earnings due to their greater rates of return.

Growth Rate

If all else stays the same, faster-growing companies tend to rely more on outside funding. Moreover, the flotation expenses related to debt sales are lower than those of ordinary stock sales. Therefore, in order to reduce financing expenses, fast-growing enterprises typically take on a little bit more debt than slower-growing ones (Barges, 2009).

Taxes

Dividends are not deductible, although interest is. Hence, the benefit of employing debt increases with a company's corporate tax rate.

Controls

When raising money, a management that is worried about control could rather issue debt than (voting) common stock. A company may sell non-voting equity shares or make a preemptive sale, allowing each shareholder to retain proportionate ownership, if certain conditions are met. Typically, a substantial worry in the process of deciding on capital structure arises only in closed-held companies or companies that are in danger of being taken over (Bhattarai, 2005).

Market Condition

Long- and short-term fluctuations in the stock and market environment can have a significant impact on a company's ideal capital structure. For instance, there was just no market for new long-term bonds at any "reasonable" interest rate during the credit crunch in the winter of 1982. When a low-rated company needed money, it had little choice except to go to the stock or short-term debt markets. Such actions are short detours from aims rather than long-term modifications to the desired capital structure.

Lenders and Rating Agency Attitude

The attitudes of lenders and rating agencies are undoubtedly significant variables in determining financial structure, even when managers analyze the appropriate leverage ratios for their companies. Most of the time, the company talks to lenders and rating agencies about its financial structure and takes their advice very seriously. However, when management is so optimistic about the future that it aims to employ leverage above and above what is customary for its sector. Such debt increases may not be accepted by lenders, or they may only be accepted at a steep cost (Pandey, 2003).

Management Attitude

Management is free to use its own discretion when determining the best capital structure to use if there is no evidence that one will result in a better stock price than another. Certain management styles lean more conservatively than others, using less debt relative to the industry norm; for other management styles, the opposite is true.

The Firm's Internal Condition

The target capital structure of a company may also be impacted by its internal circumstances. Let's say, for instance, that a company has just finished a successful R&D program and anticipates increased profits soon. Nevertheless, investors have not yet priced in the new earnings, which is why the stock price does not reflect them. This firm would like to finance itself with debt rather than issue stock until its greater earnings become apparent and are reflected in the stock price. At that point, it may choose to sell its common stock, pay off its debt, and revert back to its ideal capital structure (Bhattacharai, 2005).

Cash Flow

When contemplating a new capital structure, the company's primary focus should be on ensuring it can produce the required cash flows to cover its obligations. Any change in the capital structure must be supported by a cash forecast that shows the ability to pay down debt and preferred shares.

Contractual Obligation

Contractual restrictions may apply to the kind or source of cash that a company is able to raise in the future. A document that outlines the terms of a previous bond issue, for instance, can forbid the company from selling more debt unless the holders' interests are made subordinate to the debt that already exists. There may also be contractual restrictions on the ability to distribute stock dividends and sell new stock (Gautam & Thapa, 2004).

Timing

In a volatile market, timing decisions must be made based on anticipated developments. In the event that the company's equity stock price is now low but is anticipated to increase in response to improved performance and/or positive market developments. Utilizing debt financing initially and equity financing thereafter could be beneficial. However, in the event where the equity stock price of the company is balanced, it might be preferable to use equity financing initially and debt financing afterwards. These variables should be taken into account while formulating a financing goal regarding debt and shares. The company's management may decide to set its capital structure close to the top of such ranges in order to take full use of advantageous leverage. For further information, subject to the additional requirements listed below (Pandey, 2003).

- **Profitability:** A corporation should have the most advantageous capital structure. Leverage should be used as much as possible at the lowest possible cost given the limitations.
- **Solvency:** The company's solvency is threatened by the usage of excessive debt. If debt does not pose a substantial risk, it should be utilized; if not, it should be avoided.

- **Flexibility:** The capital structure shouldn't be rigid in order to accommodate evolving circumstances. If a scenario warrants it, a company should be able to implement its capital structure with the least amount of expense and delay necessary. Additionally, the business should be able to supply money as needed to support its lucrative endeavors.
- **Capacity:** The company's debt capacity should be taken into consideration while determining the capacity structure, and it should not be exceeded. The ability of a business to create cash flows determines how much debt it can take on. It ought to possess sufficient funds to cover interest and principal payments to creditors.
- **Control:** The capital structure should have the lowest possible risk of losing the company's control. Dilution of control is a significant worry for closely held company owners. The general characteristics of a suitable capital structure are as follows. Certain extra specific aspects may be reflected in a company's unique characteristics. When the company is first being promoted, it will need to plan its capital structure. Consequently, a capital structure decision is needed whenever money needs to be raised for financial investment.

2.1.4 Company Profitability

This is an effect or outcome of the business operations of the company, and the performance and profit of the company are directly related to the management of different financial resources and the effective use of those resources in the financing, investment, and operational activities. Since every company wants to maximize its profit, profitability has always been ranked first in the literature on finance and accounting. This is because it is the main objective of financial management. In fact, getting the best return on investment for stockholders is thought to be a moral imperative (Jensen, 2002).

Only a very lucrative business can provide its owners with a substantial return on their investment; an unprofitable business cannot endure. The ability of a business to make money is known as profitability, while the absence of income is known as a loss. Additionally, he claims that if income is created more than input costs, it is simply profitable, but if income is less than input costs, it indicates subpar performance (Hall & Weiss, 1967).

The effectiveness of businesses is crucial for stakeholders, investors, and the economy as a whole. A profitable firm can yield significant long-term profits for investors, who place a high value on the return on their investment. Increased financial profitability for a company can lead to higher employee wages, higher-quality products for customers, and more environmentally friendly production facilities. Additionally, increased profit will raise people's incomes and create job chances.

2.2 Empirical Review

Ramadan and Ramadan (2015) investigated capital structure and firm's performance of Jordanian manufacturing sector. The purpose of this study was to determine how capital structure affected the performance of Jordanian industrial companies listed on the Amman Stock Exchange between 2005 and 2013. The study was conducted on all 72 Jordanian industrial companies that were listed at ASE as of December 2013. The imbalanced cross sectional pooled Ordinary Least Square (OLS) regression model was employed in order to accomplish the current study's goal. Pecking-order theory, which states that there is an inverse relationship between borrowing and a company's profitability, is consistent with the study's findings, which indicated a statistically significant inverse effect of capital structure, as expressed by long-term debt to capital ratio, total debt to capital ratio, and total debt to total assets ratio, on the performance of the Jordanian industrial companies listed at ASE as expressed by return on asset ratio (ROA). This means that the most profitable companies rely less on borrowing to finance their cash needs.

Revathy and Santhi (2016) analyzed impact of capital structure on profitability of manufacturing companies in India. In order to determine the hypothesised relationship between capital structure variables and profitability, this study looked at the effect of capital structure on the profitability of Indian manufacturing companies. It also attempted to determine how much a company's revenue is affected by its capital structure variables. After dividing the chosen manufacturing enterprises into three groups according to two characteristics—stages and period—this study is conducted. First, manufacturing companies are divided into three stages: pioneering, growth, and consolidation. Secondly, these companies are categorized as pre- and post-merger. The purpose of this study is to verify the hypothesis that the profitability of Indian manufacturing companies was significantly impacted by capital structure

characteristics. Multi-stage sampling approaches were used to choose a sample of seventy organizations. Multiple regression analysis was performed in this study to examine the data. The study finds that the capital structure variable and profitability have a strong one-to-one relationship, and that an increase in the debt-to-equity ratio has an adverse effect on the profits of manufacturing companies listed on the Indian Bombay Stock Exchange.

Olusuyi and Felix (2017) analyzed the effect of capital structure on the financial performance of manufacturing firms in Nigeria. The impact of capital structure on the financial performance of Nigerian manufacturing companies was examined in this study. Ten manufacturing enterprises that were sampled used the secondary data from the published annual reports for the years 2008-2014 as their primary source of data. Panel data was used to assess the relationship between capital structure and financial performance. Returns on equity and return on assets were used to gauge financial performance, and the debt-to-equity ratio, asset turnover, and age of the company were used to gauge capital structure of the manufacturing firms in the sample. Multiple regression analysis was performed in this study to examine the data. This study found that the age of the firm had a negative, insignificant effect on the financial performance of the sampled manufacturing firms as measured by return on assets. In addition, asset turnover had a positive and significant effect on financial performance. Finally, the debt-to-equity ratio had a negative, statistically significant effect on financial performance. The study did find, however, that the age of the firm had a negative but statistically significant effect on the financial performance of the sampled manufacturing firms as measured by return on equity, and that the debt-equity ratio had a positive but insignificant effect on financial performance. Additionally, asset turnover had a positive but significant effect on financial performance.

Kalyani and Mathur (2018) examined impact of capital structure on profitability: with reference to select companies from oil and natural gas industry of India. The primary objective was to determine how a firm's capital structure affected its overall profitability. For this study, financial data from seven selected companies that are listed on the NSE and BSE between 2005 and 2015 was used. In this study, the non-random sampling method known as judgment sampling was used to choose the

sample. The functions linking to profitability as determined by return on assets and net profit ratio with capital structure metrics were estimated using correlations and regression analysis. Log sales, the amount of operating leverage, and asset growth are important factors in determining profitability when ROA and log assets are the dependent variables. The study also found that the degree of financial leverage, log sales, the amount of operating leverage, and asset growth have a significant relationship with the net profit ratio of the chosen companies from India's oil and gas industry.

Nasimi and Nasimi (2018) investigated effect of capital structure on firms' profitability: An empirical evidence from Pakistan stock exchange (PSX). The study's primary objective was to investigate how capital structure affects a company's profitability. We used annual panel data for 20 non-financial companies listed at the Pakistan Stock Exchange between 2009 and 2015 to investigate the link. Ordinary least squares (OLS) panel econometric technique is used to investigate the impact of capital structure on firms' profitability. One dependent variable and two independent variables are included in every multivariate regression model. The empirical results demonstrated that while debt to equity had little effect on net profit margin and return on asset, it had a large impact on return on equity. Debt to asset ratio, however, significantly affected net profit margin and return on asset but had little effect on return on equity. The study concluded that an organization's performance was influenced by the capital structure that its firms chose, and that this capital structure had a major impact on profitability. Managers should therefore take into account how debt affects a company's profitability before modifying the amount of debt in the capital structure. In addition, the lenders impose the debt covenants with consideration for how they may affect the profitability of the companies. Therefore, to achieve the desired level of efficiency and success in business performance, the capital structure should have an ideal balance of debt and equity.

Dhodary (2019) analyzed determinants of capital structure on trading and manufacturing enterprises: a case of Nepal. The primary objective of this study was to investigate the factors that influence capital structure in Nepalese manufacturing and trading companies. Secondary sources provided the data that were needed to complete the study. Financial information for ten fiscal years, from F/Y 2005/2006 to F/Y

2015/2016, for each enterprise. The study came to the conclusion that the main factors influencing corporate capital structure in Nepalese trading and manufacturing companies are asset tangibility, profitability, liquidity, and interest coverage ratio.

Rahman et al. (2019) examined the impact of capital structure on the profitability of publicly traded manufacturing firms in Bangladesh. This study looked at how capital structure affected Bangladeshi publicly traded manufacturing companies' profitability. In order to determine the association between the independent variables (debt ratio, equity ratio, and debt to equity ratio) and the dependent variables (return on asset, return on equity, and earnings per share), this study used fixed effect regression. From 2013 to 2017, a sample of 50 observations from ten manufacturing companies that were chosen and listed on the Dhaka Stock Exchange were examined. According to this study, ROA was significantly impacted positively by both the debt and equity ratios, but negatively by the debt to equity ratio. This analysis also reveals that while the debt to equity ratio significantly lowers ROE, the equity ratio significantly increases it. Lastly, the debt to equity ratio significantly reduces earnings per share. The research's conclusions will support listed manufacturing companies in maintaining an ideal capital structure, which will maximize stockholder wealth.

Mouna et al. (2019) examined the impact of capital structure on firm's performance in Morocco. The primary objective of the study was to find out how capital structure affected Moroccan enterprises' performance. The fixed effect model was used to analyze the link between capital structure and firm performance because it fit the first model better based on the Hausmann test results. The annual data, which spans three years from 2014 to 2016 and includes 53 Moroccan companies, was gathered from the official websites of the Casablanca Stock Exchange and the Moroccan Authority of Capital Market. Three explanatory variables were found to have a significant effect in the research results: size had a significant positive impact on firm performance using return on equity (ROE) as a proxy; debt ratio (DR) had a negative significant impact on return on asset (ROA); and debt equity ratio (DER) had a negative and significant impact on return on equity (ROE). Because Moroccan companies had very high financial risk, their profitability decreased as their level of leverage increased. This meant that decreasing external financing was necessary to improve their financial

performance, as the trade-off theory—which assumed a positive relationship between capital structure and firm performance—was rejected.

Jaishi and Poudel (2019) investigated capital structure and firm efficiency of non-financial institutions in Nepal. The study looked at the connection between non-financial companies' efficiency and leverage in Nepal. The basic structure of leverage and efficiency, as well as their relationship, were examined in this study using both a descriptive and informal research design. The study used secondary data, which were taken from the annual reports of the relevant companies and included 60 observations spread between two to fourteen years. Regression analysis and descriptive analysis were both utilized to evaluate the relationship between the variables. To test the hypothesis, many models were employed. Higher leveraged enterprises were inefficient, while lower leveraged firms are more productive. The expansion of non-financial institutions in Nepal, their investment in intangible assets, and their profitability do not always translate into increased productivity. The hypothesis that increased investment in tangible assets boosts a firm's efficiency is supported by the positive association between tangibility and efficiency. The main finding of this study was that the key variables influencing the efficiency and leverage of non-financial Nepalese enterprises were size, tangibility, profitability, and growth. Higher leveraged enterprises are inefficient, while lower leveraged firms are more productive.

Ayange et al. (2021) analyzed effect of capital structure on firm's performance in Nigeria. This study looked at the impact of capital structure metrics on the performance of Nigerian manufacturing firms. Using annualized panel data for fifteen listed companies from various sectoral groupings between 1999 and 2018. excluding the financial institutions because of the special nature of their capital structure and the stringent legislative constraints imposed on their options for funding. The non-financial firms are the subject of this investigation. The firm's market and book values are measured by capital structure. The findings show that while ROA has a negative impact on LDTA, D/E, and TDTA, performance proxy measured by ROE and Tobin's Q strongly influences SDTA, SIZE, LDTA, and TDTA. When compared to other book values, the results showed a strong correlation between Tobin's Q and financial performance. A more accurate indicator of performance throughout the review period is Tobin's Q. According to the study, Nigerian businesses are eager to finance

themselves with short-term debt, which validates the Pecking Order Theory. It's important to remember that the impact of capital structure on company performance cannot be adequately explained by a single hypothesis.

Ngoc et al. (2022) examined the impact of capital structure on financial performance of logistic service providers listed on Ho Chi Minh City Stock Exchange. This article's primary objective was to ascertain how capital structure affected the financial performance (measured by ROA and ROE) of logistics companies listed on HOSE between 2012 and 2019. utilizing a quantitative approach (using models of Pool OLS, FEM, REM, and FGLS) and data from 30 logistics companies registered on HOSE between 2012 and 2019. According to this study, debt to assets significantly reduced ROA. On the other hand, liquidity and tangibility significantly increased ROA. Additionally, this study discovered that tangibility, growth, and debt to assets all had little positive effects on ROE. However, the companies' ROE was negatively impacted by their size and liquidity. Thus, the study's findings demonstrated that capital structure has a detrimental effect on profitability.

Shrestha (2023) analyzed impact of capital structure on profitability of Dabur Nepal Private Limited. Examining the relationship between Dabur Nepal Private Limited's profitability and capital structure was the primary goal of the study. Descriptive statistics, Pearson correlation, regression analysis, and t-test were used to complete the data analysis. The debt-to-equity ratio (DER), debt-to-capital ratio (DCR), debt-to-total-assets ratio (DTAR), equity-to-total-assets ratio (ETAR), short-term liability to total assets ratio (SLTAR), and profitability, including return on assets (ROA), are all represented by the capital structure. The results of this study indicated that the dependent variable's positive correlation with the set of independent factors is smaller. The outcome demonstrated that the effects of DER, DCR, DTA, ETA, and SLTA on Dabur Nepal Pvt. Ltd.'s ROE are negligible.

Huong (2023) investigated effect of capital structure on the profitability of plastic and packaging companies listed in Vietnam. Analysis of the effect of capital structure on the profitability of plastic and packaging companies listed on the Vietnam Stock Exchange was the main objective of the study. Both qualitative (synthetic methods, statistical methods, descriptive methods, inductive and interpretive methods) and

quantitative (linear regression methods) research techniques were used in this study. This study discovered that the short-term debt ratio (STD) and the long-term debt ratio (LTL), two independent variables that reflect a capital structure, have a significant impact on the profitability of businesses. Based on the study's findings, the author provides financial solution ideas meant to increase businesses' profitability along with a number of debates and evaluations on the crucial function that capital structure adjustments play for plastic and packaging industries.

Thapa et al. (2023) analyzed impact of capital structure on the profitability of manufacturing companies in Nepal: a case study of Sarbottam cement Nepal. Using Sarbottam Cement Nepal as a case study, the study examined the effect of capital structure on the profitability of manufacturing firms in Nepal. In this study regression analysis was conducted to look at the connections between these factors. The debt-to-assets and debt-to-equity ratios did not significantly affect return on equity, according to the results of the regression study. In the same way, the return on assets was not substantially impacted by these ratios. Additionally, there were no statistically significant correlations found between liquidity and size and return on assets and return on equity. There was no discernible correlation between the independent variables and the profitability indicators of the Sarbottam Cement manufacturing company.

Yensu et al. (2024) investigated how does capital structure impact on profitability of listed firms of Ghana stock exchange? The primary objective of the research were to precisely examine the capital structures of a subset of the listed companies, determine the correlation between capital structure and profitability, and explore the impact of capital structure on the profitability of the listed companies in Ghana. The study used regression and correlation analysis to achieve its objectives. The correlation study's findings showed a strong positive relationship between equity and both ROA and NPM. However, there was a negative correlation found between profitability and long-term debt. The regression analysis predicts that when long-term debt rises, ROCE, ROA, and NPM would all decrease. An increase in equity will cause ROA and NPM to grow.

Chandulal and Ransariya (2024) examined the effect of capital structure on profitability: a study on Indian paper industry. Analyzing the impact of capital structure decisions on the chosen companies' profitability over a ten-year period, from 2013–14 to 2022–23, was the primary goal of this study. The debt-to-equity ratio is employed in this study as an independent variable to measure capital structure. However, gross profit margin, net profit margin, return on net worth, return on capital invested, and return on assets are utilized as dependent variables to quantify profitability. Ratio analysis, descriptive statistics, regression analysis, and correlation analysis have all been used to examine the gathered data. The study's conclusions showed that there was a negative association between capital structure and profitability in the correlation analysis. Regression analysis results, however, show that while debt to equity had a substantial impact on return on assets and return on capital employed, it had no significant effect on gross profit margin, net profit margin, or return on net worth.

Table 1

Summary of Empirical Review

S.N.	Authors	Title	Objective	Methodology	Major Findings
1	Ramadan & Ramadan (2015)	Capital structure and firm's performance of Jordanian manufacturing sector.	This study aimed to identify the effect of capital structure on the performance of the industrial Jordanian Companies listed on Amman Stock Exchange	In order to achieve the objective of the current study the unbalanced cross sectional pooled Ordinary Least Square (OLS) regression model was used.	The study's findings demonstrated a statistically significant unfavorable relationship between capital structure and the performance of Jordanian industrial companies listed at ASE. This relationship was measured by three different ratios: long-term debt to capital, overall debt to capital, and total debt to total assets.
2	Revathy & Santhi (2016)	Impact of capital structure on profitability of manufacturing companies in India.	This study examined the impact of capital structure on profitability of the manufacturing companies in India.	This study used multiple regression analysis to analyze the data.	The study discovered that the capital structure variable and profitability had a strong one-to-one relationship, and that an increase in the debt-to-equity ratio had an adverse effect on the profits of the Indian manufacturing companies listed on the Bombay Stock Exchange.
3	Olusuyi & Felix (2017)	The effect of capital structure on the financial	This research work investigated the effect of capital	This study used multiple regression analysis to	The results of this study showed that the age of the company had a negative, insignificant effect on the

		performance of manufacturing firm's in Nigeria (2008-2014).	structure on the financial performance of manufacturing firms in Nigeria.	analyze the data.	financial performance of the sampled manufacturing firms as measured by return on assets. In addition, asset turnover had a positive, significant effect on financial performance. The debt-to-equity ratio had a negative, statistically significant effect on financial performance.
4	Kalyani & Mathur (2018)	Impact of capital structure on profitability: With reference to select companies from oil and natural gas industry of India.	The main objective was to find out impact of capital structure on overall profitability of a firm.	The correlations and regression analyses were used to estimate the functions relating to profitability and capital structure.	The study discovered that when ROA and log assets are used as dependent variables, the degree of financial leverage, log sales, degree of operating leverage, and growth of asset have a significant relationship with the net profit ratio of the chosen firms. These factors are important in determining profitability.
5	Nasimi & Nasimi (2018)	Effect of Capital Structure on Firms' Profitability : An Empirical Evidence from Pakistan Stock Exchange (PSX).	The main objective of the study was to examine the impact of capital structure on firms' profitability.	Each multivariate regression model incorporates two independent and one dependent variables	The empirical results demonstrated that while debt to equity had little effect on net profit margin and return on asset, it had a large impact on return on equity. Debt to asset, however, significantly affected net profit margin and return on asset but had little effect on return on equity.
6	Dhodary (2019)	Determinants of capital structure on trading and manufacturing enterprises: A case of Nepal.	This study mainly aimed at examining the determinants of capital structure in Nepalese trading and manufacturing firms.	This study used multiple regression analysis to analyze the data.	The study discovered that the primary factors influencing corporate capital structure in Nepalese trading and manufacturing enterprises are asset tangibility, profitability, liquidity, and interest coverage ratio.
7	Rahman et al. (2019)	The impact of capital structure on the profitability of publicly traded manufacturing firms in Bangladesh.	This research explored the impact of capital structure on the profitability of publicly traded manufacturing firms in Bangladesh.	This study applied the fixed effect regression to find out the correlation among independent variables and dependent variables	According to this study, ROA was significantly impacted positively by both the debt and equity ratios, but negatively by the debt to equity ratio. This analysis also reveals that while the debt to equity ratio significantly lowers ROE, the equity ratio significantly increases it. Lastly, the debt

8	Mouna et al. (2019)	The impact of capital structure on Firms performance in Morocco.	The main objective of study was to investigate the impact of capital structure on firm's performance in Morocco.	Based on the result of Hausmann test, fixed effect fit the first model to analyze the data.	to equity ratio significantly reduces earnings per share. Using return on equity (ROE) as a proxy, the research findings indicated that size had a positive significant impact on firm performance and that the debt ratio (DR) had a negative significant impact on return on asset (ROA), the debt equity ratio (DER) had a negative and significant impact on return on equity (ROE), and the research findings indicated a significant effect of all three explanatory variables.
9	Jaishi & Poudel (2019)	Capital structure and firm efficiency of non financial institutions in Nepal. .	The study examined the relationship between leverage and efficiency of non-financial firms in Nepal.	Descriptive as well as regression analysis was used to assess the relationship among the variables.	The main finding of this study was that the key variables influencing the efficiency and leverage of non-financial Nepalese enterprises were size, tangibility, profitability, and growth. Higher leveraged enterprises are inefficient, while lower leveraged firms are more productive.
10	Ayange et al. (2021)	Effect of capital structure on firms performance in Nigeria.	This study examined capital structure measures on manufacturing firm's performance in Nigeria.	This study used the multiple regression analysis to analyze the data.	The findings showed that while ROA has a negative impact on LDTA, D/E, and TDTA, performance proxy measured by ROE and Tobin's Q strongly influences SDTA, SIZE, LDTA, and TDTA. When compared to other book value, the results showed a strong correlation between Tobin's Q and financial performance.
11	Ngoc et al. (2022)	The impact of capital structure on financial performance of logistic service providers listed on Ho Chi Minh City Stock Exchange.	The main research objective of this article was to determine the impact of capital structure on financial performance (ROA and ROE) of logistics enterprises listed on HOSE.	This study used quantitative method (with models of Pool OLS, FEM, REM and FGLS).	According to this study, debt to assets significantly reduced ROA. However, ROA was significantly improved by tangibility and liquidity. Additionally, this study discovered that tangibility, growth, and debt to assets had negligible beneficial effects on ROE. However, the companies' ROE was negatively impacted by their size and liquidity.
12	Shrestha (2023)	Impact of capital	The main objective of the	Data analysis was complete	The results of this study indicated that the dependent

		structure on profitability of Dabur Nepal Private Limited.	study was to investigate the impact of capital structure and the profitability of Dabur Nepal Private Limited.	using descriptive statistics, Pearson correlation, regression analysis, and t-test.	variable's positive correlation with the set of independent factors is smaller. The outcome demonstrated that the effects of DER, DCR, DTA, ETA, and SLTA on Dabur Nepal Pvt. Ltd.'s ROE are negligible.
13	Huong (2023)	Effect of capital structure on the profitability of plastic and packaging companies listed in Vietnam.	The study aimed to analyze the impact of capital structure on the profitability of plastic and packaging companies listed on the Vietnam Stock Exchange.	This study used statistical methods, description; inductive, interpretive methods and linear regression methods.	This study discovered that the long-term debt ratio (LTL) and the short-term debt ratio (STD) are two independent factors that indicate a capital structure that significantly influences the profitability of businesses.
14	Thapa et al. (2023)	Impact of capital structure on the profitability of manufacturing companies in Nepal: A case study of Sarbottam cement Nepal.	The study investigated the impact of capital structure on the profitability of manufacturing companies in Nepal.	Regression analysis was employed to examine the relationships between these variables.	The debt-to-assets and debt-to-equity ratios did not significantly affect return on equity, according to the results of the regression study. In the same way, the return on assets was not substantially impacted by these ratios. Additionally, there were no statistically significant correlations between liquidity and size and return on assets and return on equity.
15	Yensu et al. (2024)	How does capital structure impact on profitability of listed firms of Ghana stock exchange?	The main objective of the study was to specifically analyze the capital structure of selected listed companies	In order to accomplish its goals, the study used regression and correlation analysis.	The correlation study's findings showed a strong positive relationship between equity and both ROA and NPM. However, there was a negative correlation found between profitability and long-term debt.
16	Chandulal & Ransariya (2024)	The effect of capital structure on profitability: A study on Indian paper industry.	The main aim of this study was to analyze the effect of capital structure decision on profitability of the selected companies	The collected data has been analyzed by ratio analysis, descriptive statistics, regression analysis and correlation analysis	The study's conclusions showed that there was a negative association between capital structure and profitability in the correlation analysis. Regression analysis results, however, show that debt to equity had no discernible effect on gross profit margin, net profit margin, or return on net worth.

2.3 Research Gap

"Research gap" refers to the discrepancy between this investigation and earlier research. Firstly, there is a temporal research gap between this study and previous ones. Although they had previously researched earlier eras, their analysis covers the years 2022–2023. Subsequently, whereas earlier research likewise employed a limited time frame of no more than five years, this study covered ten years. Aside from that, the results of earlier research on the relationship between capital structure and manufacturing enterprises' profitability were few and general. In order to examine the effects of capital structure on the profitability of Nepalese manufacturing companies, this study looks at a variety of explanatory variables, including debt ratio, debt to equity ratio, and company size, as well as dependent variables like profitability (return on equity and return on assets). This study attempted to apply the t-test and the multicollinearity test in addition to using descriptive, correlation, and multiple regression analyses that were not examined for data analysis. Furthermore, since those manufacturing businesses were left out by the previous researchers, this study has focused on three manufacturing companies: Unilever Nepal Limited, Dabur Nepal Privated Limited, and Himalayan Distillery Limited. For this reason, this work makes a significant effort to close the research gap.

CHAPTER – III

RESEARCH METHODOLOGY

The methodical process of solving an issue by systematic information gathering, recording, analysis, interpretation, and reporting regarding the various aspects of a phenomenon under study is known as research methodology. The procedures and methods used throughout every facet of the investigation are described in the research methodology for this work. Research design is divided into four sections: research framework, variable definitions, population and sample, sampling design, nature and sources of data, data collection tool, and analytic approach.

3.1 Research Design

Research design is a plan of structure and strategy of investigation conceived so as to obtain answer to research questions and to control variances. To achieve the specific objective of the study, descriptive and causal comparative research design have been carried out in terms of impact capital structure on profitability of manufacturing companies in Nepal. Descriptive research design is adopted for analyzing position of capital structure whereas causal comparative research design is followed to analyze the relationship and impact of capital structure on profitability of manufacturing companies.

3.2 Population and Sample, and Sampling Design

Nowadays a number of manufacturing companies have been emerging rapidly. Some have already been established and others are in the process of establishment. There are all together 118 manufacturing companies operating in Nepal (Ministry of Industries, 2022-23). In this study, all the manufacturing companies are population of the study. Among them Unilever Nepal Limited, Dabur Nepal Private Limited and Himalayan Distillery Limited are selected as sample on the basis of purposive sampling method because these three companies are top three in profitability in the present context.

3.3 Nature and Sources of Data, and the Instruments of Data Collection

This study used only secondary data. The data is taken from annual reports of related manufacturing companies and their websites. Secondary data are those data that are collected by someone else or used already and made available to other in the form of published statistics. So, the major sources and types of data include these published sources such as annual reports of the manufacturing companies, various theses related to this study and NRB reports, books, journals and articles etc.

3.4 Method of Analysis

Arithmetic Mean

The simple mean, or arithmetic mean, of a set of data is calculated by dividing the total number of observations by the sum of all the observations. The arithmetic mean of a variable is the best value that represents the group as a whole. Arithmetic mean of a series is given by:

$$\text{Mean } (\bar{X}) = \frac{\sum X}{n}$$

Where,

\bar{X} = denotes arithmetic mean, n denotes the no. of periods and x_1, x_2, \dots, x_n are the individual observations.

Standard Deviation

The positive square root of the mean squared of the departure from the arithmetic mean is the definition of the standard deviation. It displays the ranges and magnitudes of deviations from the mean or center. It gauges the dispersion in absolute terms. The variability will increase with a higher standard deviation and vice versa. Dispersion quantifies how much the data deviate from the central value. Put differently, it is beneficial to examine the data's quality in terms of its variability. It is calculated as:

$$\text{Standard Deviation (SD)} = \sqrt{\frac{\sum (X - \bar{X})^2}{n}}$$

Co-efficient of Variation

The standard deviation represents the dispersion in absolute terms. The measurement of the coefficient of standard deviation is the relative measure of dispersing depending

on the standard deviation. Coefficient of variation is the percentage measure of coefficient of so. More homogeneity and consistency with fewer CVs, and vice versa. Standard deviation alone is inappropriate when comparing two sets of data; nevertheless, CV can also compare two variables separately based on their variability. It is calculated as under:

$$\text{Coefficient of Variation (C.V.)} = \frac{\sigma}{\bar{X}} \times 100$$

Coefficient of Correlation

The relationship between the independent and dependent variables is known as the correlation coefficient. It is a technique for ascertaining how these two variables are related to one another. A correlation coefficient is present when there is a strong relationship between the two variables, meaning that changes in the independent variable's value also affect the dependent variable's value.

$$\text{Correlation Coefficient (r)} = \frac{n\Sigma XY - \Sigma X \Sigma Y}{\sqrt{n\Sigma X^2 - (\Sigma X)^2} \sqrt{n\Sigma Y^2 - (\Sigma Y)^2}}$$

Regression Analysis

Regression analysis is a collection of statistical procedures used in statistical modeling to estimate the relationships between variables. When examining the link between a dependent variable (ROA and ROE) and one or more independent variables (debt ratio, debt to equity ratio, and firm size), it encompasses a variety of modeling and analysis methodologies. More precisely, regression analysis clarifies how, when any one of the independent variables is changed while the other independent variables are kept constant, the usual value of the dependent variable, also known as the "criterion variable," varies.

Model Specification

The model is simple linear regression function that links the ratio of capital structure and profitability variables. The general regression equation is of the form:

$$\text{Model 1: } ROA_{it} = \beta_0 + \beta_1 DER_{it} + \beta_2 DAR_{it} + \beta_3 SIZE_{it} + e_{it} \quad (1)$$

$$\text{Model 2: } ROE_{it} = \beta_0 + \beta_1 DER_{it} + \beta_2 DAR_{it} + \beta_3 SIZE_{it} + e_{it} \quad (1)$$

Where:

ROA_{it} = Return on assets of manufacturing company i^{th} for the time period t

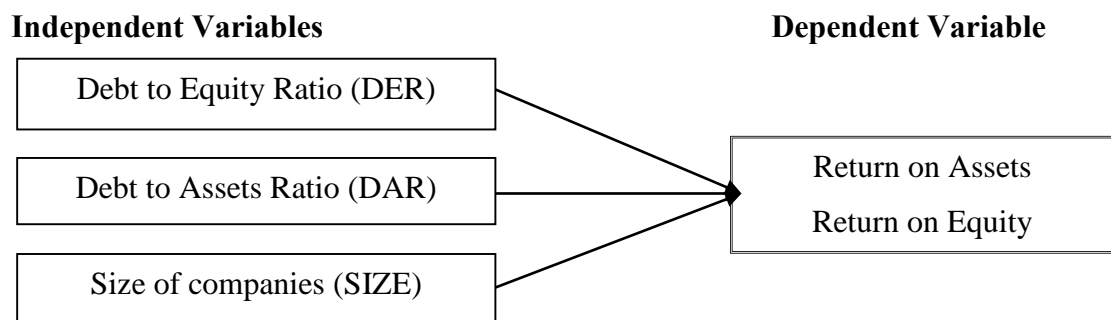
ROE_{it} = Return on equity of manufacturing company i^{th} for the time period t
 DER_{it} = Debt to equity ratio of manufacturing company i^{th} for the time period t
 DAR_{it} = Debt to assets ratio of manufacturing company i^{th} for the time period t
 $SIZE_{it}$ = SIZE of manufacturing companies i^{th} for the time period t
 β_0 = The intercept (constant)
 $\beta_1, \beta_2, \beta_3$ = Regression coefficient of independent variables.
 e = error component.

3.5 Research Framework and Definition of Variables

From the theoretical and empirical literature reviews, the following conceptual framework of the study is developed by the researcher.

Figure 1

Research Framework of the Study



Source: Revathy and Santhi (2016); Olusuyi and Felix (2017); Mouna, Jianmu, Havidz and Ali (2019); Rahman, Sarker and Uddin (2019) and Ayange et al. (2021)

Independent Variables

Debt to Equity (D/E) ratio

It shows the percentage of long-term debt financing a company's equity. It's a debt ratio meant to gauge the financial leverage of an organization. It shows the ratio of a company's debt to equity held by shareholders in relation to the amount of debt used to finance its assets. A higher debt-to-equity ratio indicates that the business has used debt financing aggressively. Excessive risk is frequently linked to aggressive leveraging strategies. The extra interest payment could cause earnings to fluctuate as a result. Ayange et al. (2021) found that debt to equity ratio had insignificant negative effect on ROA of manufacturing companies. Likewise, Rahman et al. (2019); Mouna et al. (2019) found debt to equity ratio had negative impact on ROA.

$$\text{Debt-equity ratio} = \frac{\text{Total Debt}}{\text{Total Shareholder's equity}}$$

Debt to Asset (D/A) ratio

It is the percentage of long-term debt used to finance an organization's assets. An organization is more leveraged and therefore at more risk financially if its debt to asset ratio is higher. Better financial performance with less or moderate reliance on debt is indicated by a smaller debt to asset ratio, whereas a larger ratio shows a greater reliance on debt. Rahman et al. (2019) debt to assets ratio (DTR) had positive impact on ROA. At the same time, Revathy and Santhi (2016) found that debt to assets ratio had positive impact on ROA.

$$\text{Debt-total assets ratio} = \frac{\text{Total Debt}}{\text{Total assets}} \times 100$$

Size of Companies (SIZE)

One control variable that could have an impact on a firm's value that isn't determined by its leverage is its size. The proxy for the size of the company was the logarithm of total assets. Huong (2023); Ngoc et al. (2022) concluded that size of companies had positive impact on ROA. However, Mouna et al. (2019); Kalyani and Mathur (2018) had significant negative impact on profitability of manufacturing companies in Nepal. Size of companies (SIZE) = Log of total asset

Dependent Variables

Return on Asset (ROA)

Return on assets is first dependent variable in this study. It was used by Kalyani and Mathur (2018); Rahman et al. (2019); Mouna et al. (2019). A financial ratio called return on asset (ROA) indicates the percentage of profit an organization makes in comparison to its total resources. ROA provides a solution to the query: what can you accomplish with the resources at your disposal? The management is better when the ROA is higher. Managers, investors, or analysts might use return on assets (ROA) to gauge how effectively a company's management is generating profits from its assets.

$$\text{Return on Asset (ROA)} = \frac{\text{Net Profit}}{\text{Total Assets}}$$

Return on Equity (ROE)

The amount of net income returned as a percentage of shareholder equity is known as return on equity. Revathy and Santhi (2016); Sarker and Uddin (2019); Mouna et al. (2019) used ROE as dependent variables in their studies. It assesses a company's profitability by disclosing the amount of profit it makes on the capital that shareholders have contributed. In light of this, how Nepalese manufacturing businesses operate and how the factors included in this study relate to one another, as well as how much profit a company earns for every share of equity held by its shareholders.

$$\text{Return on Equity (ROE)} = \frac{\text{Net Profit After tax}}{\text{Total Equity}}$$

CHAPTER - IV

RESULTS AND DISCUSSION

The main objective of this study is to ascertain how capital structure affects the profitability of Nepalese manufacturing enterprises, as the researcher covered in the earlier chapters. Consequently, the three sections that make up this chapter are devoted to the outcomes and analysis of the findings. Descriptive and correlation analyses of the study's variables were reported in the first section; the assumptions of the linear regression model were fulfilled in the second; and the regression's findings were presented in the third. For additional statistical analysis, the ratio of the designated dependent and independent variables, as well as the ratio scale measurement, were computed using data analysis techniques. The collected data was analyzed by the aid of the statistical software SPSS version 26.

4.1 Results

4.1.1 Position and Status of Variables

In this section, five principle indicators such as debt to equity ratio, debt to total assets ratio, size of companies, return on assets and return on equity are analyzed.

4.1.1.1 Debt to Equity

This ratio assesses the relative positions of outsiders and the owner with regard to the company's assets. The total debt to equity ratio illustrates the relative contributions of debt capital and equity capital funds to the entire investment. A high ratio, relative to the owners, means that a larger portion of the funding comes from the creditors, who want a low debt-to-equity ratio. An equal share of the company's assets is owned by investors and creditors when the debt to equity ratio is one. A reduced debt to equity ratio is frequently associated with a company's perception as being safer and more stable financially.

Table 2*Debt to Equity*

	(In times)		
Year	HDL	UNL	DNL
2013/14	0.89	0.58	0.49
2014/15	1.34	0.57	1.43
2015/16	0.57	0.61	1.30
2016/17	0.76	0.49	1.00
2017/18	0.51	0.60	1.00
2018/19	0.42	0.66	0.81
2019/20	0.59	0.66	0.60
2020/21	0.13	0.89	0.68
2021/22	0.12	0.82	0.59
2022/22	0.09	0.59	0.53
Mean	0.54	0.65	0.84
SD	0.39	0.12	0.33
CV	71.92	18.75	39.17

Source: Appendix- I

Table 2 shows that the debt to equity ratio of manufacturing companies is in fluctuating trend. The highest debt to equity ratio of DNL is 1.43 percent in the fiscal year 2014/15 during the study period and the lowest ratio of 0.09 percent of HDL in the fiscal year 2022/23. The highest average ratio of DNL is 0.84 but the lowest average ratio of HDL which is 0.54 times. It indicates that having a low debt to equity ratio is preferable. Among the sample companies, HDL has a more strong financial position. UNL has the lowest risk among the sample manufacturing companies since it has the lowest standard deviation of all of them. UNL has been the most constant in the ratios, with the lowest coefficient of variation (18.75 percent) among them, according to the ratios.

4.1.1.2 Debt to Assets Ratio

By dividing the total debt of the company by the total value of its assets, this ratio is computed. Both current and fixed assets make up the firm's total assets, and both long- and short-term debt make up its total debt. It shows the percentage of total assets financed by creditors, liabilities, and debt. If the company's total debt to asset ratio is 100 percent, then it has the same amount of obligations as assets. A manufacturing company with a total debt to asset ratio more than 100 percent is said to have more obligations than assets. A lower overall debt to asset ratio makes a

corporation riskier since it suggests that it has more assets than liabilities and might have to sell those assets to pay off debt in an emergency.

Table 3

Debt to Assets

	(In Percent)		
Year	HDL	UNL	DNL
2013/14	47.12	36.88	32.86
2014/15	57.20	36.11	58.90
2015/16	36.12	37.96	56.49
2016/17	43.02	32.74	50.07
2017/18	33.66	37.55	50.09
2018/19	29.57	39.81	44.68
2019/20	37.24	39.74	37.59
2020/21	11.48	47.01	40.40
2021/22	10.89	45.19	36.98
2022/22	8.57	37.08	34.65
Mean	31.49	39.01	44.27
SD	16.50	4.25	9.23
CV	52.41	10.90	20.85

Source: Appendix- I

Table 3 shows that the debt to assets ratio of manufacturing companies is in variable trend. The highest debt to assets ratio of DNL is 58.90 percent in the fiscal year 2014/15 during the study period and the lowest ratio of 8.57 percent of HDL in the fiscal year 2022/23. The highest average ratio of DNL is 44.27 but the lowest average ratio of HDL which is 31.49 percent. The higher the ratio, the higher the degree of leverage. Depending on averages ratio, investing in DNL may lead to a higher risk than in other companies. Because UNL has the lowest standard deviation of all the sample companies, it carries the least amount of risk. Based on the ratios, UNL has shown to be the most consistent, having the lowest coefficient of variation (10.90 percent) of all of them.

4.1.1.3 Size of the Companies

The decimal logarithm of the manufacturing companies' total assets is used to calculate the size of the company. Given that larger businesses have greater resources, better risk diversification, more sophisticated information systems, and more effective expense management, a positive correlation between company size and profitability is predicted.

Table 4
Size of the Companies

(Rs. in Lakhs)			
Year	HDL	UNL	DNL
2013/14	9497	23577	37583
2014/15	11310	28135	44959
2015/16	9593	30464	45592
2016/17	10179	32031	49707
2017/18	12007	33218	92862
2018/19	14036	38302	92549
2019/20	19956	38572	93963
2020/21	23097	47376	109629
2021/22	31924	58047	124058
2022/22	36693	64951	140606
Mean	17829.20	39467.30	83150.80
SD	9850.84	13398.45	36574.61
CV	55.25	33.95	43.99

Source: Appendix – I

Table 4 shows that the size of manufacturing companies in Nepal. The size of the manufacturing companies is in increasing trend except of HDL. The average size of DNL's total assets is 83150.80 lakhs, while HDL's firms have the lowest average size at 17829.20 lakhs. It suggests that DNL is the greatest corporation, with the most risk diversification, sophisticated information systems, and most effective expenditure control out of all of them. HDL has the lowest standard deviation among the sample firms, indicating that it carries the least amount of risk. Based on the coefficient of variation of the ratios, UNL has demonstrated the highest level of consistency, with the lowest CV of 33.95 percent.

4.1.1.4 Return on Assets

A crucial profitability statistic called return on assets calculates a manufacturing company's earnings per rupee of its assets. It demonstrates the company's capacity to turn a profit without the need for leverage. Therefore, return on assets provides insight into how well management uses firm assets to generate profit, but often, shareholders are more interested in other financial ratios, like return on equity, than in return on assets alone. The contribution of assets to the creation of net profit is explained by return on total assets. This ratio shows how effectively assets are managed. This ratio aids management in determining the variables that impact the company's overall success.

Table 5*Return on Assets*

	(In percent)		
Year	HDL	UNL	DNL
2013/14	13.76	39.21	28.24
2014/15	7.18	38.58	9.98
2015/16	25.95	36.65	2.92
2016/17	4.80	36.82	10.18
2017/18	24.49	29.06	8.29
2018/19	38.26	31.60	7.40
2019/20	23.40	27.62	5.79
2020/21	45.08	9.88	6.11
2021/22	33.11	18.11	10.35
2022/22	18.00	26.56	9.77
Mean	23.40	29.41	9.90
SD	13.01	9.50	6.88
CV	55.60	32.31	69.42

Source: Appendix – I

Table 5 shows that the return on assets of manufacturing companies in Nepal. The ratio of the sample companies are in fluctuating trend. UNL has the highest average return on assets (294.1%), while DNL has the lowest average ratio (9.90%). The fact that UNL had the greatest ratio among them suggests that they were able to manage their entire operations. Put another way, UNL maximizes the return on its assets by making the best use of the asset that has the biggest impact on the overall mean of ROA. DNL has the lowest standard deviation among the sample firms, indicating that it carries the least amount of risk. Based on the coefficient of variation of the ratios, UNL has demonstrated the highest level of consistency, with the lowest CV of 32.31 percent.

4.1.1.5 Return on Equity

To determine whether an owner's investment is profitable, a return on shareholder equity is computed. A company's profitability is gauged by its return on equity (ROE), which shows how much profit the company makes on the capital that shareholders have invested. Net profit after taxes is calculated and divided by shareholder equity to determine the return on equity.

Table 6*Return on Equity*

	(In percent)		
Year	HDL	UNL	DNL
2013/14	26.03	62.12	42.06
2014/15	16.77	60.38	24.28
2015/16	40.62	59.07	6.71
2016/17	8.43	54.74	20.38
2017/18	36.92	46.53	16.61
2018/19	54.32	52.50	13.38
2019/20	37.28	45.84	9.28
2020/21	50.93	18.65	10.25
2021/22	37.15	33.05	16.43
2022/22	19.69	42.22	14.96
Mean	32.81	47.51	17.43
SD	14.82	13.60	10.11
CV	45.17	28.62	57.97

Source: Appendix – I

Table 6 shows that the return on equity of manufacturing companies in Nepal. The ratio of the sample companies are in fluctuating trend. UNL has the highest average return on equity (47.51 percent), while DNL has the lowest average ratio (17.43 percent). The idea is that the UNL's return on equity represents the best or most efficient management in terms of profit-making among them all. Furthermore, UNL is performing in a progressive manner. DNL has the lowest standard deviation among the sample companies, indicating that it carries the least amount of risk. Based on the coefficient of variation of the ratios, UNL has demonstrated the highest level of consistency, with the lowest CV of 28.62 percent.

4.1.2 Descriptive Statistics of Variables

The descriptive statistics of the variables used in the study have been presented in Table 7. The result shows that the minimum and maximum of performance measure in terms of profitability indicators ROE and ROA along with other independent variables of manufacturing companies in Nepal.

Table 7*Descriptive Statistics of Variable of Manufacturing Companies*

Variables	N	Minimum	Maximum	Mean	Std. Deviation
DER	30	.09	1.43	.6773	.31897
DAR	30	8.57	58.90	38.2550	12.04298
LSIZE	30	3.98	5.15	4.5502	.33837
ROA	30	2.92	45.08	20.9050	12.80930
ROE	30	6.71	62.12	32.5860	17.69867

Source: Appendix –II

Table 7 shows the descriptive statistics of dependent and independent variables used in the study. The first independent variables debt to equity ratio, the average ratio is 0.6773 times and standard deviation of 0.31897 over the study period with the maximum ratio at 1.43 percent and the minimum this ratio being positive 0.09 percent. Likewise, the second independent variables debt to assets ratio shows that this ratio varies from a minimum of 8.57 percent to a maximum of 58.90 percent with an average of 38.2550 percent and standard deviation of 12.04298. The last independent variables size of companies shows that this ratio varies from a minimum of 3.98 to a maximum of 5.15 with an average of 4.5502 and standard deviation of 0.33837. The summary of ROA shows that the average return on assets over the study period is 20.9050 percent and standard deviation of 12.80930, the maximum return on assets is 45.08 percent and the minimum of 2.92 percent. The return on assets shows how efficient the manufacturing companies are using its assets to generate profit measured by profit before interest and tax divided by total assets. ROE mean is 32.5860 percent from the range to minimum 6.71 to maximum 62.12 percent. Then, standard deviation for ROE is 17.69867.

4.1.3 Correlation Analysis

A correlation matrix is a table that shows the correlation coefficients between variables. Each table cell shows the correlation between two matched variables. A correlation matrix is a useful tool for summarizing data. This provides us with a brief summary of the variables that exhibit varying degrees of importance and correlation. The absence of a linear relationship between the two variables is indicated by a correlation value of 0. A perfect positive relationship is represented by a correlation coefficient of +1, while a perfect negative relationship is represented by a correlation coefficient of -1. In Table 8, the correlation matrix is displayed as follows.

Table 8*Pearson Correlation Coefficients of Study Variables*

	DER	DAR	LSIZE	ROA	ROE
DER	1				
DAR	.960**	1			
LSIZE	.056	.087	1		
ROA	-.628**	-.594**	-.366*	1	
ROE	-.450*	-.381*	-.373*	.962**	1

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

* . Correlation is significant at the 0.05 level (2-tailed).

Source: Appendix-III

Table 8 reveals the correlation test between both dependent and independent variables using correlation coefficient matrix. The correlation test shows that debt equity to equity ratio (DER) has significant negative relation with ROA in 5 percent level of significance with correlation coefficients -0.628. At the same time, debt to equity ratio has also significant negative relation with ROE. Similarly, there is significant negative correlation between debt to total assets ratio and ROA and also significant negative relationship between debt to total assets ratio and ROE. Further, size of companies has significant negative relationship with ROA and it has also significant negative relationship with ROE of the manufacturing companies.

4.1.4 Regression Analysis

It includes many techniques for modeling and analyzing several variables, when the focus is on the relationship between dependent variables (ROA and ROE) and independent variables (debt to equity ratio, debt to total assets ratio, and size of companies). Ordinary least square regression (OLS) of panel data analysis is used as a major tool of analysis.

4.1.4.1 Analysis of Return on Assets Regression

ROA is the dependent variable and independent variables are debt to equity ratio, debt to total assets ratio, and size of companies to analyze the effect of capital structure on profitability of manufacturing companies.

Table 9*Model Summary*

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.713 ^a	.509	.452	9.47869

a. Predictors: (Constant), LSIZE, DER, DAR

Source: Appendix-IV

The R square is 0.509. The implication therefore is that, 50.90 percent of the variation in the dependent variable (ROA) is explained by the independent variables (debt to equity ratio, debt to total assets ratio, and size of companies). The R statistic in this study, which is 0.713, shows that the study variables have a high association with one another. This suggests that the independent variables have a significant impact on return on equity. Regression analysis is perfectly correlated with standard error of estimate.

Table 10*Analysis of Variance (ANOVA)*

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	2422.281	3	807.427	8.987	.000 ^b
Residual	2335.983	26	89.845		
Total	4758.264	29			

a. Dependent Variable: ROA

b. Predictors: (Constant), LSIZE, DER, DAR

Source: Appendix-IV

An examination with ANOVA (F-value) indicates that explains the most possible combination of predictor variables that could contribute to the impact of dependent variables. Results show significant impact of ROA indicator. On the F-values of 8.987 ($p = 0.000 < 0.05$) for LSIZE, DER, DAR as ROA proxy, it clearly shows that there is a significant relationship between the dependent variable (ROA) and the independent variables.

Table 11*Regression Coefficient of Independent Variables with ROA*

Variables	Coefficients	t-statistics	Sig. or p-value
(Constant)	92.242	3.802	.001
DER	-34.442	-1.737	.094
DTR	.276	.523	.605
LSIZE	-12.867	-2.453	.021

Source: Appendix-IV

Table 11 presents the regression coefficient of independent variables debt to equity ratio, debt to total assets ratio, and size of companies and the intercept value of dependent variable ROA. The regression result of debt to equity ratio (DER) has a negative relationship with ROA by a coefficient estimate of -34.442. This means that holding other independent variables constant and when one times increases in debt to equity ratio (DER), consequently it decreases ROA of the manufacturing companies by -34.442 percent and the p value of debt to equity ratio (DER) is 0.094 reveal that it is statistically insignificant at 5 percent level of significance. Accordingly, the result supports the working hypothesis that debt to equity ratio (DER) has insignificant negative effect on ROA of manufacturing companies.

The results of regression model indicated that the relationship between debt to assets ratio (DAR) has a positive relationship with ROA by a coefficient estimate of 0.276. This means that holding other independent variables constant and when one percent increases in debt to assets ratio (DAR), as a result it increases ROA of the manufacturing companies by 0.276 percent and the p value of debt to assets ratio (DAR) is 0.605 discloses that it is statistically insignificant positive effect on ROA of manufacturing companies at 5 percent level of significance.

The result of regression shows that the relationship between size of companies (SIZE) has a negative relationship with ROA by a coefficient estimate of -12.867. This means that holding other independent variables constant and when one percent increases in size of companies (SIZE), as a result it decreases ROA of the manufacturing companies by -12.867 percent and the p value of size of companies (SIZE) is 0.021 discloses that it is statistically significant at 5 percent level of significance. This means size of companies has significant negative impact on ROA of manufacturing companies in Nepal.

4.1.4.2 Analysis of Return on Equity Regression

ROE is the dependent variable and independent variables are debt to equity ratio, debt to total assets ratio, and size of companies to analyze the effect of capital structure on profitability of manufacturing companies.

Table 12

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.612 ^a	.375	.302	14.78132

a. Predictors: (Constant), LSIZE, DAR, DTR

Source: Appendix-V

The R square is 0.375. The implication therefore is that, 37.50 percent of the variation in the dependent variable (ROE) is explained by the independent variables (debt to equity ratio, debt to total assets ratio, and size of companies). The R statistic in this study, which is 0.612, shows that the study variables have a moderate association with one another. This suggests that the independent variables have a moderate impact on return on assets. Regression analysis is perfectly correlated with standard error of estimate.

Table 13

Analysis of Variance (ANOVA)

Model	Sum of Squares	df	Mean Square	F	Sig.
1 Regression	3403.376	3	1134.459	5.192	.006 ^b
Residual	5680.672	26	218.487		
Total	9084.048	29			

a. Dependent Variable: ROE

b. Predictors: (Constant), LSIZE, DER, DAR

Source: Appendix-V

An examination with ANOVA (F-value) indicates that explains the most possible combination of predictor variables that could contribute to the impact of dependent variables. Results show significant impact of ROE indicator. On the F-values of 5.192 ($p = 0.006 < 0.05$) for LSIZE, DER, DAR as ROE proxy, it clearly shows that there is a significant relationship between the dependent variable (ROE) and the independent variables.

Table 14*Regression Coefficient of Independent Variables with ROE*

Variables	Coefficients	t-statistics	Sig. or p-value
(Constant)	121.820	3.220	.003
DER	-66.964	-2.166	.040
DAR	1.191	1.451	.159
LSIZE	-19.653	-2.402	.024

Source: Appendix-V

Table 14 presents the regression coefficient of independent variables debt to equity ratio, debt to total assets ratio, and size of companies and the intercept value of dependent variable ROE. The regression result of debt to equity ratio (DER) has a negative relationship with ROE by a coefficient estimate of -66.964. This means that holding other independent variables constant and when one times increases in debt to equity ratio (DER), consequently it decreases ROE of the manufacturing companies by -66.964 percent and the p value of debt to equity ratio (DER) is 0.040 reveal that it is statistically significant at 5 percent level of significance. Hence, debt to equity ratio (DER) has significant negative effect on ROE of manufacturing companies.

The results of regression model indicated that the relationship between debt to assets ratio (DAR) has a positive relationship with ROE by a coefficient estimate of 1.191. This means that holding other independent variables constant and when one percent increases in debt to assets ratio (DAR), as a result it increases ROE of the manufacturing companies by 1.191 percent and the p value of debt to assets ratio (DSR) is 0.024 discloses that it is statistically significant positive impact on ROE of manufacturing companies at 5 percent level of significance.

The result of regression shows that the relationship between size of companies (SIZE) has a negative relationship with ROE by a coefficient estimate of -19.653. This means that holding other independent variables constant and when one percent increases in size of companies (SIZE), as a result it decreases ROE of the manufacturing companies by -19.653 percent and the p value of size of companies (SIZE) is 0.024 discloses that it is statistically significant at 5 percent level of significance. This means size of companies has significant negative impact on ROE of manufacturing companies in Nepal.

4.2 Discussion

The main objective of this study is to investigate the impact of capital structure on profitability of manufacturing companies. Capital structure has impact on return on assets and returns on equity, the two main parameters for measuring profitability of the manufacturing companies in Nepal. The correlation analysis shows that debt equity ratio (DER) has significant negative relation with ROA. This finding is similar with the previous study of Rahman et al. (2019). This result is also consistent with the finding of Kalyani and Mathur (2018); Ramadan and Ramadan (2015) mentioned that debt to equity ratio had negative relationship with ROA.

At the same time, debt to equity ratio has also significant negative relation with ROE which is consistent with the finding of Rahman et al. (2019); Kalyani and Mathur (2018). Then, there is significant negative correlation between debt to total assets ratio and ROA which is similar with the finding of Rahman et al. (2019); Ramadan and Ramadan (2015). Likewise, debt to total assets ratio has also significant negative relationship between debt to total assets ratio and ROE. This is similar with the finding of Rahman et al. (2019) which observed that debt to assets ratio had significant negative relationship with ROE. Moreover, size of companies has significant negative relationship with ROA which is similar with the finding of Kalyani and Mathur (2018); and it has also significant negative relationship with ROE of the manufacturing companies which is similar with the finding of Kalyani and Mathur (2018).

The multiple regression analysis found that debt to equity ratio (DER) has insignificant negative effect on ROA of manufacturing companies which is similar with the finding of Ayange et al. (2021); Rahman et al. (2019); Mouna et al. (2019); Olusuyi and Felix (2017); Revathy and Santhi (2016); Ramadan and Ramadan (2015). However, it contradicts with the finding of Kalyani and Mathur (2018) concluded that debt to equity ratio had positive impact on ROA. Then, debt to assets ratio (DTR) has an insignificant positive impact on ROA at 5 percent level of significance which is similar with the finding of Rahman et al. (2019); Revathy and Santhi (2016). However, it contradicts with the prior study of Huong (2023) found that debt to assets ratio had positive impact on ROA. This finding is also inconsistent with the finding of Ayange et al. (2021) Ngoc, Tien and Thu (2022); Mouna et al. (2019); Ramadan and

Ramadan (2015). In addition, size of companies has significant negative impact on ROA of manufacturing companies in Nepal which is consistent with the finding of Mouna et al. (2019); Kalyani and Mathur (2018) but opposite to the finding of Huong (2023) concluded that size of companies had positive impact on ROA. This is also opposite to the finding of Ayange et al. (2021) Ngoc et al. (2022).

On regression ROE, debt to equity ratio (DER) has significant negative effect on ROE of manufacturing companies. This is similar with the finding of Ayange et al. (2021) mentioned that debt to equity ratio had significant negative effect on ROE of the companies. This is also consistent with the finding of Rahman, Sarker and Uddin (2019); Mouna et al. (2019); Revathy and Santhi (2016) but opposite to the finding of Kalyani and Mathur (2018); Olusuyi and Felix (2017). The debt to assets ratio (DTR) has statistically insignificant positive impact on ROE at 5 percent level of significance. This is similar with the finding of Ngoc et al. (2022) Ayange et al. (2021); Rahman et al. (2019); Mouna et al. (2019) but opposite to the finding of Huong (2023) found that debt to assets ratio had significant negative impact on ROE. This is also inconsistent with the finding of Revathy and Santhi (2016). The result of regression also shows that size of companies has significant negative impact on ROE of manufacturing companies in Nepal. This is similar with the finding of Ngoc et al. (2022; Kalyani and Mathur (2018). However, it contradicts with the finding of Huong (2023); Ayange et al. (2021); Mouna et al. (2019) concluded that size had positive effect on ROE of the companies.

CHAPTER – V

SUMMARY AND CONCLUSION

5.1 Summary

Manufacturing businesses must make critical decisions about their capital structure in order to optimize shareholder value since these decisions should have an impact on the companies' capacity to compete. Selecting the best mix of debt and equity to maximize value while lowering financing costs is a crucial decision for today's business managers. Without a question, the financial sector contributes significantly to the economic growth of every nation. As a result, corporate success is essential to a country's overall financial stability as well as to maximizing value for its owners. To attain an ideal capital structure, manufacturing companies must select and modify their strategic financing mix to optimize value and make sure their operations are not excessively geared or under geared. Since achieving value maximization and risk minimization is not unique to Nepalese manufacturing businesses, the focus of this study is on determining how capital structure and profitability are related.

The main objective of this study is to analyze the impact of capital structure on profitability in manufacturing companies in Nepal. The specific objectives are to analyze the existing position of capital structure of manufacturing companies in Nepal, to examine the relationship between capital structure variables and profitability of manufacturing companies in Nepal and to assess the impact of debt to equity ratio, debt to assets ratio and size of companies on profitability of manufacturing companies in Nepal. Relevant journals, articles, related websites etc. are also used for this research. To achieve the specific objective of the study, descriptive and casual comparative research design has been carried out. Descriptive design is used to analyze the position of capital structure and profitability. Causal comparative research design is used to measure the impact of capital structure on profitability of manufacturing companies in Nepal. Out of total population of 118 manufacturing companies in Nepal, only three manufacturing companies are taken as sample on the basis of purposive sampling method because these companies are top three in terms of profitability in the present context as well as availability of data. Annual reports and other publications from the basis of secondary data are used. The secondary data has been collected mainly through the loan department and the annual reports of the

manufacturing companies, covering ten year periods, i.e. from the fiscal year 2013/14 to 2022/23. In this study, descriptive analysis, correlation analysis and multiple regressions are applied by using SPSS version 26. This study used ROA and ROE as dependent variables and debt to equity ratio, debt to total assets ratio and size of companies are as explanatory variables.

This study shows that manufacturing companies have great contribution to investors fund and strong capital adequacy position due to high debt to equity ratio. Moreover, in this study, manufacturing companies shows a large share of financing by the insurers relatively to the owners and there is risky for the investors due to the high leverage ratio or debt equity ratio. Profitability is the measurement of efficiency. Manufacturing companies have high value of ROA and ROE means there is efficient utilization of its total assets. Investors are getting more return from their investment and also company performance is good. The correlation analysis shows that debt to equity ratio (DER) and debt to total assets have significant negative relation with profitability (ROA and ROE) of manufacturing companies in Nepal. Moreover, size of companies has significant negative relationship with profitability (ROA and ROE) of the manufacturing companies. The regression result reveals that debt to equity ratio has insignificant negative effect on ROA but it has significant negative impact on ROE of the manufacturing companies while debt to assets ratio has insignificant positive impact on profitability (ROA and ROE) of manufacturing companies. Further, size of companies has significant negative impact on profitability (ROA and ROE) of the manufacturing companies in Nepal. Hence, this study concluded that capital structure has insignificant impact on profitability of manufacturing companies in Nepal.

5.2 Conclusion

Based on this analysis, this study concluded that that manufacturing companies' success in exploiting debts to the high profitable assets due to the high debt to assets ratio and owners of the companies always prefer a high debt ratio. It is meant that manufacturing companies have great contribution to investors fund and strong capital adequacy position. Moreover, in this study, manufacturing companies shows a large share of financing by the investors relatively to the owners and there is risky for the insurers due to the high leverage ratio or debt equity ratio. Profitability is the

measurement of efficiency. It indicates the degree of success in achieving desired profit. It shows entire performance of companies. Manufacturing companies have high value of ROA and ROE means there is efficient utilization of its total assets. Investors are getting more return from their investment and also company performance is good. So, it can be concluded that manufacturing companies has strong capital adequacy position and strong profitability position.

The correlation analysis shows that debt to equity ratio (DER) has significant negative relation with profitability (ROA and ROE) of manufacturing companies in Nepal. Likewise debt to assets ratio has also significant negative relation with ROA and ROE. Further, size of companies has significant negative relationship with profitability (ROA and ROE) of the manufacturing companies. So, it can be said that there is significant negative relationship between capital structure and profitability of manufacturing companies in Nepal.

The regression result shows that debt to equity ratio has insignificant negative impact on ROA but it has significant negative impact on ROE of the manufacturing companies. However, debt to assets ratio has insignificant positive impact on profitability (ROA and ROE) of manufacturing companies. Moreover, size of companies has significant negative impact on profitability (ROA and ROE) of the manufacturing companies in Nepal. Therefore, it can be concluded that capital structure has insignificant impact on profitability of Nepalese manufacturing companies.

5.3 Implications

The investigation has produced the following guidelines for enhancing the impact of capital structure on Nepalese manufacturing firms' profitability.

- This study found that debt to equity ratio has insignificant negative impact on ROA but it has significant negative impact on ROE of the manufacturing companies. However, debt to assets ratio has insignificant positive impact on profitability (ROA and ROE) of manufacturing companies. Moreover, size of companies has significant negative impact on profitability (ROA and ROE). In this regard, the outcomes of this study are expected to provide additional and valuable information regarding the impact of capital structure on profitability.

As a result, it signals to policymakers and manufacturing company management to make every financial decision feasible.

- Some of the most recent information, statistics, and concerns about capital structure and profitability may be found in this research. As a result, investors or stockholders should find this study important.
- The study's conclusions are beneficial to investors and future researchers. This paper is a valuable resource for future researchers.
- This study suggests that more research be done on this topic over the course of more than ten years, using a sample size of more than three manufacturing companies and other financial institutions like commercial banks, finance companies, development banks, and microfinance, insurance companies among others. If done correctly, this could yield stronger results for the goal of implementing policy. Furthermore, only three independent variables the debt to equity ratio, the size of the companies, and the debt to assets ratio were examined in this study. Therefore, further research needs to be done by including other specific factors such as liquidity ratio, long term debt to equity ratio, equity to total assets ratio, tangible assets and macroeconomic variables such as GDP growth rate and inflation rate etc.

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ABSTRACT This study investigates effect capital structure

on profitability of manufacturing companies in Nepal. Secondary data was gathered from manufacturing companies of Nepal for ten year periods

(2013/14-2022/23).