CORPORATE GOVERNANCE AND LEVERAGE DECISIONS OF NEPALESE LISTED NON-FINANCIAL COMPANIES

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Exam Roll No. 230/17

TU Registration No. 6-3-38-652-2012

A Graduate Research Report submitted to in partial fulfillment of the requirements for the degree of

MASTER OF FINANCE AND CONTROL

at the

School of Management

Faculty of Management

Tribhuvan University

Kirtipur, Kathmandu

July 2022

RECOMMENDATION

CERTIFICATION

We, the undersigned, certify that we have read and hereby recommend for acceptance by the SOMTU, Tribhuvan University, a Graduate Research Project (GRP) report submitted by Ms. Manju Lekhak entitled **"CORPORATE GOVERNANCE AND LEVERAGE DECISIONS OF NEPALESE LISTED NON-FINANCIAL COMPANIES"** in partial fulfillment of the requirements for the award of the degree of Master of Finance and Control of Tribhuvan University.

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DECLARATION OF AUTHENTICITY

I, Manju Lekhak, declare that this GRP is my own original work and that it has fully and specifically acknowledged wherever adapted from other sources. I also, understand that if at anytime it is shown that I have significantly misrepresented material presented to SOMTU, any credit awarded to me on the basis of that material may be revoked.

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ACKNOWLEDGEMENT

The Graduate Research Project entitled “Corporate Governance and Leverage Decisions of Nepalese Listed Non-Financial Companies” has been prepared to fulfill the partial requirement for MFC degree of Tribhuvan University.

First of all, I would like to express my sincere gratitude to my supervisor Mr. Sanjay Ghimire for his valuable guidance and support that has helped me to accomplish this project.

I would also like to extend my deepest gratitude to all my friends and family who directly or indirectly helped me to complete this GRP.

I would like to thank the School of Management, Tribhuvan University for providing an opportunity to carry out Graduate Research Project which has enhanced my knowledge about research and report writing.

Finally, I would like to express my appreciation and sincere gratitude to all the faculty members and administration team of School of Management, Tribhuvan University for their direct and indirect moral support.

Sincerely,
Manju Lekhak
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ABBREVIATIONS

ROA	Return on Assets
TIE	Times Interest Earned
BOD	Board of Director
NEPSE	Nepal Stock Exchange
NPV	Net Present Value
GLS	Generalized Least Squares
CEO	Chief Executive Officer
S&P 500	Standard and Poor's 500
EBIT	Earnings Before Income and Tax
OECD	Organization for Economic Cooperation and Development
GMM	Generalized Method of Moments
SET	Securities Exchange of Thailand

EXECUTIVE SUMMARY

The graduate research project entitled “Corporate Governance and Leverage Decisions of Nepalese Listed Non-Financial Companies” is a descriptive research study.

A comprehensive literature review was conducted in which the necessary information, articles, journals and theories related to capital structure was reviewed and discussed. The main objective of the study is to examine the effect of corporate governance measures (ownership concentration, board size and board composition) on the leverage decisions of Nepalese non-financial companies listed in NEPSE while controlling for some firm-specific characteristics like firm size, firm age, ROA, current ratio and tangibility. Two measures of leverage i.e. debt ratio and TIE ratio were taken as dependent variables. For this, 30 non-financial companies were taken as sample from 59 non-financial companies excluding the sectors categorized as others by NEPSE. The data was collected from secondary source such as annual reports and website of the companies for the fiscal year 2019-20. Analysis was done using descriptive statistics, correlation and regression analysis.

The study found that the model as a whole was significant. The variables were empirically tested by stepwise multiple regression analysis. The findings revealed that there is significant but negative impact of board size on leverage as measured by debt ratio. The board composition and ownership concentration are found to have insignificant impact on the leverage (debt ratio) of the companies.

The study has identified that except ownership concentration, board size and board composition have significant impact on the leverage of the companies as measured by TIE ratio.

CHAPTER I
INTRODUCTION

1.1 Background of the Study

Governance is the process or act of governing. Thapa (2008) defined corporate governance as a strategy used by companies to achieve their goals. In corporate sector it is defined as the method used to direct or control the organization. Corporate governance is described by the OECD (2004) as a system of interactions between a company's management, board of directors, shareholders, and other stakeholder groups. In short it is a collection of institutional value, entity's, culture and regulations that affect how a firm is run or governed. A company's performance is directly impacted by how well its corporate governance is doing. It is found that those organization where corporate governance is taken seriously and who have governed their affairs effectively have prospered.

By managing corporate affairs, corporate governance generates value for shareholders. Corporate governance, which includes the structure of the board and its operating processes, refers to corporate decision-making and control. It is a network of connections between the management, board, shareholders, and stakeholders of an organization. With the ultimate goal of maximizing profitability and long-term shareholder value, corporate governance assists in controlling and managing a company's business operations.

The structure through which firms are managed and directed is known as corporate governance, and the board of directors is in charge of it. The shareholders' responsibility in corporate governance is to select the directors and auditors and to ensure that an effective governance framework is in place.(Cadbury, 1992). The severe repercussions, including catastrophic losses of financial institutions that nearly brought about the financial system's collapse and the subsequent deep global recession in 2009, highlight the significance of corporate governance (Lang & Jagtiani, 2010).

Strategic decisions related to external financing are affected by good corporate principles. The strategic decisions made at the board level of a firm, such as external

financing, financing costs, and other matters, are significantly influenced by good corporate governance standards. Corporate governance is the top-level control structure made up of the senior management and the board of directors, who have the authority to make decisions (Jensen, 1993). Hence, factors affecting corporate governance, such as board size, board independence, the CEO/chair dual role, may directly affect choices regarding leverage or capital structure.

The segregation of ownership and control of the corporation is the primary cause of the agency problem, which is typically linked to corporate governance. The interactions between shareholders and managers give rise to agency issues, which are based on conflicts of interest within the company. Similar to this, another issue with corporate governance is the clash of interests between minority and majority owners. Agency cost is one of the factors that affect capital structure, according to contemporary theories of corporate finance.

Capital structure, also known as financial structure, explains various ways used by a company in buying its assets. It is the combination of debt and equity maintained by an organization. It refers to a way in which a company finances its assets, overall operations and growth through some combination of equity and debt. Debt of a company may include both short-term and long-term debt, while equity includes common stock, preferred equity and reserves and surplus (retained earnings). When analyzing a company's leverage, the ratio of short-term to long-term debt is taken into account, which provides insight into how risky a company is. A company has to make a critical decision of designing an appropriate capital structure. The financial structure of a company is very crucial as it is associated with the ability of the company to meet the needs of its shareholders and other concerned authorities.

Modigliani and Miller were the scholars to address the issue of financing structure at first. They claimed that financial structure of a company is independent and irrelevant in determining a company’s worth and its future performance. Over the last six decades, the issues considering financial structure has been dominated by the famous irrelevance hypothesis proposed by Modigliani and Miller in 1958. A company should be unconcerned whether a project is financed with debt or equity as “the average cost of capital to any firm is completely independent of its capital structure and is equal to the

capitalization rate of a pure equity stream of its class" (Modigliani & Miller, 1958, pp. 268-269).

Since then, many capital structure theories have emerged which do not operate on the "irrelevance model" of capital structure, which makes the assumption of perfect capital markets. Such theories are based on the assumption that company's choice of capital structure depends upon trade off theory. These arguments center on the agency costs associated with using debt and equity to finance projects (Jensen & Meckling,1976) and the utilization of debt to communicate information about the future prospects of the firms to stakeholders (Ross, 1977). Hence, it is evident that financial structure of the firm have influence on performance of the firm and its value.

1.2 Statement of the Problem

The importance of corporate governance in an organization has increased public interest in recent years. Nowadays organization should not only focus on profit but it also should emphasize on ethical dealing and incorporate best corporate governance practices. Even though several research has been conducted in this area before, the majority of the studies on corporate governance focuses on describing the business performance and factor. A detailed analysis of the literature shows that empirical research is concentrated on the effect of corporate governance on business performance. However, the connection between corporate governance and aspects of corporate finance like capital structure has not yet been thoroughly investigated. There are limited studies that have discussed how the corporate governance affects organization's financing policies. In contrast to popular capital structure theories like trade-off theory, pecking order theory, and market timing theory, this research emphasizes the significance of how enterprises are managed and how this effects financial policy.

This study aims to investigate how corporate governance practice effect financing choices made by non-financial companies listed on the NEPSE. In this context, the study has raised the following research questions:

- What is the effect of board size on debt ratio and TIE ratio of non-financial companies listed in NEPSE?

- What is the effect of board composition on debt ratio and TIE ratio of non-financial companies listed in NEPSE?
- What is the effect of ownership concentration on debt ratio and TIE ratio of non-financial companies listed in NEPSE?

1.3 Research Objectives

The main objective of this research is to analyze the impact of corporate governance on capital structure or leverage decisions of non- financial companies listed in NEPSE.
More specifically, the objectives are as follows:

- To evaluate the impact of board size on leverage.
- To examine the impact of board composition on leverage.
- To analyze the impact of ownership concentration on leverage.

1.4 Hypotheses

The following hypotheses have been formulated for the study:

Board Size and Leverage

Adams and Mehran (2003) described that larger board can oversee management's actions and provide good corporate administration than smaller board. In contrast, Lipton and Lorsch (1992) asserted that boards with small number of directors are more effective and efficient than bigger ones and that larger boards waste resources. Companies with a large number of board members have minimal leverage, claim Berger et al. (1997). However, Jensen (1986) discovered that companies with bigger boards have high leverage. Similar findings were made by Wen et al. (2002), who discovered a positive correlation between board size and financial structure, but the connection is statistically not significant. Board size and leverage for Ghanaian enterprises were found to be significantly positively correlated by Abor (2007) and Bokpin and Arko (2009). The majority of the literature hypothesized a positive association between board size and leverage, despite the conflicting facts on the subject. Hence, the first hypothesis has been formulated as follows:

$H_{1.a}$: Board size will have positive relationship with debt ratio.

$H_{1.b}$: Board size will have positive relationship with TIE ratio.

Board Composition and Leverage

The variable board composition measures the percentage of outside directors in the board. Independent or outside directors can closely monitor the actions of the management and adopt the necessary governance measures when there is a high level of board independence. Independent directors can bring new insights and also specific expertise from their sector and personal experience to the management of a company. Weisbach (1988) asserts that when independent directors are in charge of the board of directors, top managers are effectively monitored. Wen et al. (2002) showed negative but significant relationship between proportion of independent directors and financial structure. They argued that since independent directors generally keep an eye on managers more closely, managers choose to use less leverage to avoid the added risk that comes with utilizing more leverage.. Abor (2007) , Berger et al. (1997) and Jensen (1986) found that outside directors' percentage on the board and firm's leverage ratio have a strong positive relationship. The independent directors assures management accountability to shareholders and lessens clash between shareholders and managers, which result in high debt policies. Furthermore, companies with higher proportion of independent directors ensure good governance and can raise debt capital more easily than other companies suggesting that companies with higher proportion of independent directors have high leverage and vice versa. It seems that firms with more independent directors employ higher leverage as they have easier access to credit in the market. Hence, the second hypothesis is proposed as follows:

$H_{2.a}$: Board composition will have positive relationship with debt ratio.

$H_{2.b}$: Board composition will have positive relationship with TIE ratio.

Ownership Concentration and Leverage

The concentration of shares held by shareholders affects the capital structure of a firm. Compared to minor shareholders, large owners have a larger investment in the company and assume more risk. Major shareholders are motivated to keep an eye on and direct management to safeguard their sizeable fund (Friend & Lang, 1988; Mehran, 1992). It is suggested that having large shareholders or outside block holders will limit managerial opportunism and lessen agency conflicts between management and shareholders (Shleifer & Vishny, 1986). Short et al. (2002) provided empirical evidence that suggested negative relationship between ownership concentration and

leverage. According to Santos et al. (2014), ownership concentration and capital structure have a negative relationship. They discovered that the negative impact was brought on by the monitoring effect of debt's monitoring effect, the risk aversion of large block holders, and the substitution effect of ownership concentration to leverage. Because managers' decisions are impacted by the major shareholders in organizations with a concentration of ownership, agency costs are shown to be low in these firms.. On the other hand, Brailsford et al. (2002) found a positive association between ownership concentration and financial structure. They discovered that the debt favorability is explained by the monitoring impact of debt. Margaritis and Psillaki (2010) also found a positive significant effect of ownership concentration on leverage. Shareholders with concentrated ownership can direct their companies by determining their leverage. Associating ownership concentration with high debt levels, shareholders typically prefer debt financing in the businesses to control and oversee managers' activities. Many academics concur that in order to maintain control over the company and prevent ownership erosion, shareholders prefer debt financing over equity financing. Hence, the third hypothesis is formulated as follows:

$H_{3.a}$: Ownership concentration will have positive relationship with debt ratio.

$H_{3.b}$: Ownership concentration will have positive relationship with TIE ratio.

1.5 Significance of the Study

The study provides empirical evidence on corporate governance and financing choices of non-financial companies of Nepal. This research aims to investigate how good corporate governance system affect the leverage decisions of non-financial companies listed on Nepal Stock Exchange. The study is intended to contribute to the prevailing literature of board structure and capital structure by analyzing the effect of corporate governance variables on leverage decisions. Existing studies in Nepal focus on the association between board structure and leverage decisions in Nepalese listed financial companies and there has been few studies to cover the non-financial companies. This study is helpful in filling this research gap.

1.6 Limitations

- This study has not been able to include all the non-financial companies listed in Nepal Stock Exchange due to data unavailability.

- There are many attributes of corporate governance but only three of them is considered in the study.
- The study has used cross sectional analysis due to data unavailability.

1.7 Structure of the Study

The study comprises of three main sections: preliminary sections, body of the report and supplementary section. The preliminary section consists of the page, certificate declaration of authenticity, acknowledgement, table of contents, list of tables and figures, abbreviations used and executive summary. The body of the report is further divided into five chapters: introduction, related literature and theoretical framework, research methodology, analysis and results, and discussion, conclusion and implications. The final section of the report comprises of bibliography, appendix.

The overall background of the study, problem statement, hypotheses, significance of the study, limitations and structure of the study have been included in the first chapter of introduction.

The second chapter is concerned with review of related literature and theoretical framework. It consists of the findings of the previous research related to the current study. Different research works related to effect of corporate governance on leverage decisions are discussed in order to prepare a base for the study. Further, the chapter consists of theoretical framework defining each dependent and independent variable based on previous literatures.

The third chapter discusses research methodology used for the study, which comprises of research design, population and sample, sources of data, collection of methods, and finally data analysis tools and techniques.

The analysis of the study and results are shown in fourth chapter. It comprises of various tables, figures intended to answer the research question of the study.

The last chapter deals with discussion, conclusion and implications of the study. Under the discussion part, comparisons of previous findings and present study are conducted. At last, conclusion and implication are drawn out.

Finally, the supplementary section comprises of references and appendix that have been incorporated in the study.

CHAPTER II
RELATED LITERATURE AND THEORETICAL FRAMEWORK

The main objective of this chapter is to review research that have been done on corporate governance and capital structure. It reviews the theories underpinning the concept of capital structure. The empirical evidences regarding the effect of corporate governance on leverage decisions of firms that has contributed to the field of study are highlighted in this study. Theoretical framework has been developed based on the review of literature. This chapter, therefore, attempts to provide a comprehensive literature review of the various relevant and prominent studies conducted in the concerned area of study.

2.1 Theories of Capital Structure

Various capital structure theories have been created over time, each of which has a unique way of explaining how decisions about financing are made and how the capital structure is composed. There are conflicting opinions regarding whether or not capital structure or leverage decision affects the value of the organization.

2.1.1 Modigliani and Miller Theorem

Modigliani and Miller (1958) reveals the company's worth is independent of how it is financed. Two businesses with the same worth but different financial structures, one funded entirely by equity and the other by a mix of equity and debt, have same value. They claimed a company's potential to make profits and the underlying value of the assets it owns are what determine its value (Modigliani & Miller, 1958). Additionally, Modigliani and Miller (1958) created the ideal capital market and best replacement assumptions for leverage. In addition, there are no taxes, transaction costs, agency costs, bankruptcy costs, or expenses associated with asymmetric knowledge.

In 1963, Modigliani and Miller published a follow-up paper in which they updated their perspective on the leverage and added corporate income taxes. They said that enterprises with and without leverage are not valued equally. Because interest payments are tax deductible, protecting the company's pre-tax income, the value of a levered firm

is higher than that of an unlevered one. The added value of a leveraged firm over an unlevered firm is the amount of tax saved (Modigliani & Miller, 1963).

2.1.2 Trade-off Theory

Kraus and Litzenberger (1973) explained that the decision to choose the capital structure of the company depends on the advantage of borrowing with cost associated with it. Kraus and Litzenberger (1973) stated a company's market value is not dependent on its capital structure in a complete and ideal capital market. They did, however, add that the taxation of corporate profits and the existence of bankruptcy expenses are market flaws that have an impact on the market value of the companies. The tax shield enables businesses to deduct interest expenses from gross earnings, which lowers net profit and lowers tax liability. A company might theoretically borrow an unlimited sum of money and benefit from doing so. However, as the firms' financial commitments grow and the likelihood of financial trouble rises due to debt repayment and interest on the debt. (Kraus & Litzenberger, 1973).

2.1.3 Pecking Order Theory

According to Myers and Majluf's pecking order theory, the capital structure is influenced by three types of finance: internal financing, debt, and equity. Managers choose internal finance over debt and equity financing over each other. Asymmetric information is the cause of this pecking order. It is considered that management is more knowledgeable than potential investors about the firm's value. Investors logically interpret the firm's behavior. Under these presumptions, an equilibrium model of the issue-invest decision is built, which demonstrates that enterprises may refuse to issue stock and, as a result, may miss out on worthwhile investment opportunities. It describes a number of elements of how corporations behave when it comes to finance, such as their propensity to rely on internal resources of funding and their preference for debt over equity when seeking external financing (Myers & Majluf, 1984).

2.1.4 Agency Theory

According to Jensen and Meckling's agency theory, managers do not always act in their owners' best interests. They claimed that management have their own agendas, and shareholder wealth maximization is not always given top priority. Agency costs may

result from differences in managers' and owners' interests resulting from each party's self-interest or from disparities in the information available(Jensen & Meckling, 1976). Overinvestment is common example. According to Jensen (1986), managers have incentives to grow their companies larger than is necessary. Growth boosts managers' authority by giving them more resources to work with. Due of the strong correlation between compensation modifications and sales growth, it is also linked to increases in managers' pay. Perquisite consumption is another typical example of an agency cost. In this case, managers use the company's free cash flow on things like luxury automobiles and opulent offices that benefit them personally.

Investment on luxurious assets by managers is an example of agency cost that directly result in the loss of shareowners' money. Monitoring expenses and bonding costs are further examples of agency costs (Jensen,1986). Costs associated with keeping an eye on management and determining if their decisions are appropriate for the shareholders are known as monitoring costs. Bonding costs are expenses incurred to make sure a company's management acts in the best interests of its shareholders. Examples of bonding expenses include excellent compensation, bonuses, and share-based compensation.

Agency cost can be decreased by altering the company's capital structure, or by increasing the firm's leverage and luring in debt investors (Jensen,1986). Due to the weight of interest payments and principal repayment on managers, the cash flow is reduced at their discretion, which reduces the cost of agency. The holders of debt, in particular, have a monitoring and regulating impact. In order to ensure payment of interest and loan repayment, creditors monitor behavior of the manager and impose restrictions on it through debt covenants (Jensen,1986).

The possible clash of interest between a firm's owners and its creditors, however, results in agency costs of debt. Conflict of this kind may result in poor investment decisions, such as underinvestment and asset substitution. When shareholders demand that management replace lesser risk assets with greater risk venture, assets substitution occurs (Jensen & Meckling,1976). Equity holders' profit from an investment's surplus when it generates a high return. Debt holders assume the risk when there is low return on investment (below the face value of the debt). Debtors choose low risk, low return

investments, while shareholders favor high risk, high reward initiatives (Harris & Raviv, 1991). Therefore, it causes debt holders to be reluctant to engage in some positive NPV projects that they perceive to be overly risky. Another outcome of this tension is underinvestment, where investors turn down worthwhile initiatives because the loan holders would reap the rewards while the equity investors would receive insufficient profits. The agency costs of debt are the expenses associated with the conflict between shareholders and debt holders. According to agency theory, shareholders borrow money to safeguard their investment.

2.2 Empirical Evidences

A board of directors should include no more than ten members in order to facilitate more effective discussions. The directors in the board will know each other well and can reach to an agreement from their discussions much faster. Because some directors may take advantage of the work of others without contributing their own, large boards are less effective than small boards. The ability of a corporation to gain recognition from external stakeholders is significantly improved with independent directors. This lowers business uncertainty and improves the company's capacity for raising capital. Higher gearing levels are the result of having large number of outside directors on the board. (Lipton & Lorsch, 1992).

Jensen (1993) states the challenges of organizing and managing a sizable number of directors have a negative impact on the board's ability to provide advice and take part in long-term planning. Boards' performance can be enhanced by keeping them compact. Ineffectiveness increases and control by the CEO becomes simpler for boards with more than seven or eight members.

Regression models were applied by Yermack (1996) for 452 big public companies using data from 1984 to 1991. He discovered that the size of the board and firm value are inversely related. He provided data supporting beliefs that smaller boards of directors are more efficient. Companies with smaller boards also have more favorable financial ratio values and offer tighter management oversight.

The existing literature on board size and capital structure has produced a variety of results. Leverage and board size were found to be significantly inversely correlated by Berger et al. (1997). Larger boards of directors tend to have lower leverage ratios. Larger boards frequently put management under pressure to seek out lower leverage in order to improve performance. They discovered that CEOs with fewer board members are less entrenched because they are being watched by the board and seek out higher leverage, indicating a negative relationship between number of directors on the board and financial structure.

According to Wiwattanakantang (1999), number of directors on the board and leverage are adversely correlated, but association is statistically negligible. Empirical data on the factors influencing the capital structure of non-financial enterprises recorded on the SET in 1996 were reported in the study.

Between 1996 and 1998, Wen et al. (2002) looked into the connection between a few board features and the leverage of 60 companies of China. The empirical results indicated that smaller boards of directors result in lesser leverage in businesses. Board size and leverage have a positive correlation, but the correlation is statistically insignificant. It becomes more difficult to obtain a decision-making consensus as the number of board members rises, which could lead to weaker corporate governance. When faced with poor corporate governance, managers prefer larger debt levels. When they are not subject to greater corporate control, they take the risk associated with higher leverage.

On 226 businesses registered on the LSC Official List for the years 1988-1992, Short et al. (2002) examined the connections between debt ratios, management ownership, and large external shareholders. The study used the Friend and Lang (1988) definition, which states that external shareholders are regarded as large if they own 10% or more of equity shares. The findings demonstrated a negative relationship between debt ratio and ownership by large external shareholders. It was inferred that having a large shareholder reduces the agency costs of equity since they are more likely to engage in monitoring activities. Large external shareholders reduce the necessity of using a high degree of debt to make sure that management does not eat up excessive perquisites.

49 companies recorded ASC between 1989 and 1995 were the subject of an Brailsford et al. (2002) investigation for finding the relationship between shareholders structure and capital structure. The result demonstrated that there is a statistically significant association between equity ownership distribution among external block holders and leverage. Leverage and external block ownership are positively correlated. This is consistent with the active monitoring hypothesis. It explains that large shareholders have greater motivation to oversee the activities of management which decreases debt to a lower level .

A negative correlation between board size and debt financing costs was discovered by Anderson et al.(2004). The board of directors is in charge of supervising, assessing, and punishing the management of the organization. Greater oversight of the financial accounting process is provided by larger boards. They demonstrated the link between a larger board and lower debt financing costs. A larger board leads to a cheaper cost of debt, which encourages the use of additional debt. A sample of 252 industrial companies from the S&P 500 and the Lehman Brothers Fixed Income database were used in the study. According to the findings, large boards should embrace a high debt policy to increase the firm's worth.

47 listed companies on the Nairobi Stock Exchange (NSE) were studied by Kyereboah-Coleman and Biekpe (2006) to determine how corporate governance characteristics affected their financing decisions over a five-year period from 1999 to 2003. The regression model used was the random-effects GLS panel data model. They discovered that companies with bigger boards use more debt to increase company value, regardless of the maturity period.

Board size and leverage for Ghanaian businesses were shown to be significantly positively correlated, according to Abor (2007). All the companies that were listed on the Ghana Stock Exchange between 1998 and 2003 made up the sampling units for this study. The management of the business and its operations is under the purview of the board of directors. Given the strong correlation between board size and capital structure, larger boards may choose to implement a high debt strategy in order to increase the company's value. Additionally, the findings show that board composition

and leverage have a favorable connection. Outside directors are seen as a means of supervising, punishing, and, if required, replacing operational management.

Aljifri and Moustafa (2007) looked at the impact of various corporate governance methods on the achievement of 51 companies listed on the ABSM. The result showed that board size has a detrimental, although insignificant, impact on business performance. According to this, if the companies do not choose its board members carefully, it could result in a lack of coordination, poor communication, and issues with decision-making.

Bokpin and Arko (2009) looked at the impact of corporate governance and ownership structure on financial structure decisions made by organizations listed on the GSE for the years 2002 to 2007. They found a strong correlation between board size and capital structure for Ghanaian companies, which suggests that directors will generally substitute equity for long-term debt when deciding how much leverage to use. They did, however, observe negligible correlations with other leverage indicators.

Using multivariate regression analysis under fixed effect model approach, Butt and Hasan (2009) looked at the relationships between corporate governance, ownership structure, and capital structure for 58 randomly chosen non-financial listed companies from the KSE for the years 2002 to 2005. The debt-to-equity ratio and number of directors on the board are found to be negatively correlated, suggesting that boards having large number of directors may enforce on managers to adopt lower leverage and improve business performance. Presence of outside directors on the board do not significantly affect the financial structure. It might be because in family-owned businesses, outside directors are frequently chosen nominees of the controlling shareholders or representatives of financial institutions.

G.C. and Adhikari Rijal (2010) examined the connection between a few corporate board characteristics and the capital structure of companies registered on the NEPSE from 2002 to 2005. Since the capital adequacy requirement of the Nepal Rastra Bank regulates the capital structure of banks and financial institutions, financial institutions have been omitted from the sample. Firm-level fixed-effects panel data approach was used in the study. The empirical findings indicated that board size and leverage have a

negative, statistically insignificant relationship. Companies with more directors may be better able to convince management to use less leverage to lessen exposure to financial risk. Leverage is projected to have a negative association with the number of non-executive directors on the board. The control variables firms' age and size are statistically significantly in influencing how much debt a firm uses. Profitability was found to be a statistically negligible predictor of the debt ratio, nevertheless. The association between age of the firm and capital structure was shown to be negative and significant, indicating that as a corporation ages, it requires less external debt financing. More profitable businesses tend to use larger levels of debt because they have easier access to debt due to their stronger capacity for debt servicing. A statistically significant and positive correlation between firm size and capital structure was observed. The results indicated that more debt is employed in organization's capital structure when the size of organization is large. One explanation is that larger companies can sustain high debt ratios because they are more diversified and have lower earnings variance. Because larger organizations are thought to have lower levels of risk, lenders are more inclined to lend to them. Whereas smaller organization can find it more expensive to address information asymmetry with lenders and may therefore favor lower debt levels.

In Malaysia, Saad (2010) looked into how well public listed firms were following the corporate governance code of best practices and how that related to the capital structure of the company. Multiple regression analysis was used to gather data from annual reports of businesses and Thompson DataStream for a sample of 126 businesses from 1998 to 2006. The study found a convincing relationship between board size and the firm's capital structure after the Malaysian Institute of Corporate Governance began enforcing its best techniques for public listed companies in 2001. This was an effective response to the Asian financial crisis that began in the middle of 1997.

Sheikh and Wang (2012) looked into how leverage decision of non-financial firms listed on the KSE between 2004 and 2008 was affected by corporate governance. The findings showed a positive relationship between board size and leverage ratio. The resource dependence argument, which contends that bigger boards have greater capacity to raise money from outside sources in order to increase the worth of the company, is consistent with the positive association between board size and capital structure.

Using multiple regression analysis, Hussainey and Aljifri (2012) investigated the relationship between board structure and leverage for a sample of seventy one UAE companies registered in the Abu Dhabi securities market in 2006. They discovered that board size had no discernible impact on capital structure decisions.

Ahmadpour et al. (2012) analysed the association between capital structure and board structure of 311 companies registered on the TSE between 2005 and 2010. The results demonstrated a positive association between number of directors and capital structure. However, there was no discernible connection between board independence and capital structure.

In 113 listed businesses on the CSE, Wellalage and Locke (2012) looked into the relationships between corporate governance and capital structure choices. Data analysis is done by using a dynamic panel GMM estimation. The findings indicated that, at a 1% level of significance, independent directors' presence is inversely correlated with leverage. This is consistent with the findings of Jensen (1986) and Wen et al. (2002) that managers use lower level of leverage because they are subject to strict oversight by independent boards. Furthermore, the findings showed that ownership concentration has no significant impact on determining Sri Lankan firms' leverage. Additionally, the outcomes demonstrated that board size has no bearing on leverage ratio.

According to Heng et al. (2012), the capital structure and board of directors for 75 non-financial prominent Malaysian businesses listed on the KLSE from 2005 to 2008 were examined. The results revealed a statistically significant inverse association between number of directors on the board and leverage, as well as a significant positive association between independent non-executive directors and the firm's capital structure. According to the data, prominent corporations in Malaysia between 2005 and 2008 adopted a lower debt policy when the board was larger and a higher debt policy when there were more independent directors on the board.

Boroujeni et al.(2013) examined the effects of board structure and shareholder's structure on the leverage decision of 87 businesses registered on the TSE between 2001 and 2009. Board size and board's independence, the measures of corporate governance, are positively and negatively related with financial structure respectively.

Ganguli (2013) looked at how shareholder's structure affected the leverage decision of 81 listed medium sized companies in India between 2005 to 2009 with the exception of the banking and finance sectors, which have financial characteristics that are very different from others. These companies represented nearly all of the country's major economic sectors. The sample selection procedure made sure that the top 50 equities by market capitalization were excluded. Small businesses, which make up 75% of the market value starting from the bottom, are also excluded. The process of choosing the sample avoided including outliers, or businesses that were too large or little in terms of market value. The findings revealed that leverage has a negative relationship with diffuseness of ownership but a favorable relationship with concentrated shareholding.

Agyei and Owusu (2014) used descriptive, correlation, and multivariate regression analysis to examine the impact of shareholder's structure and board structure on the leverage decisions of eight randomly chosen manufacturing companies listed on the GSE from 2007 to 2011. They found size of board and composition of board are significantly positively related with leverage ratio. The existence of outside directors has strong effect on capital structure as the non-executive directors are generally representatives of financial institutions.

Santos et al. (2014) investigated the relationship between shareholder's concentration and gearing level of 694 Western European companies over the period 2002 to 2006. The results supported a negative relationship between leverage and ownership concentration. Lower debt levels result from more ownership concentration in the hands of the largest block holder.

Masnoon and Rauf (2014) investigated the impact of board structure on gearing level of 30 non-financial companies registered in KSE from 2009 to 2011. Data is collected from annual reports of companies. OLS regression is used for data analysis. It showed that number of directors on the board is positively related with leverage and is statistically significant indicating that it is easier to generate outside funds for firms with larger board size as banks consider firms with large board reliable, safer and secure. Board composition is statistically insignificant and negatively related to leverage ratio suggesting that large number of outside directors in the board results in lower debt. Ownership concentration has negative but statistically significant

relationship with leverage ratio. The control variables used in this study are profitability and tangibility of assets. Profitability has negative and statistically significant relationship with leverage. Tangibility of assets has negative and statistically insignificant relationship with leverage.

Farooq (2015) examined the impact of ownership concentration on gearing structure for all non-financial companies listed at MENA stock exchanges between 2005 and 2009. According to the findings, businesses with more concentrated ownership typically have low debt ratios.

Hermassi et al. (2016) evaluated the impact of board structure and shareholding structure on gearing level of non-financial companies listed on the Toronto Stock Exchange/ S&P Composite Index during the period 2008 to 2011. Financial companies are excluded from the sample as they have different financial structure. The final sample consisted of 117 Canadian companies operating in energy, industrial, materials, consumer staples, consumer discretionary, utilities, telecommunications services, health care, and information technology. The data was gathered from company annual reports and management proxy circulars. The findings showed that total number of directors and the number of outside directors in the board have no significant effect on Canadian companies' debt. However, board size is positively associated with leverage only for strongly indebted companies. A random effect Tobit regression was applied to estimate the effect of board structure on gearing level in strongly and weakly indebted companies.

Shafana (2016) conducted research on the impact of board structure on gearing decisions of top 50 turnover non-financial companies ranking on Lanka Monthly Digit 100 of Sri Lanka business magazine for the financial year 2014/15 with turnover above Rs. 8200 million for the year and are registered on the CSE. The duration of the research was 2011 to 2015 and used multiple panel regression model for investigating the objectives of the study. The findings of the study revealed that number of directors and outside directors have no significant effect on gearing decision for the period 2011 to 2015 in non-financial companies having higher turnover, less total assets and higher profitability.

Granado-Peiró and López-Gracia (2016) investigated the connection between capital structure and corporate governance of 89 non-financial enterprises registerd on the SSE from 2005 to 2011. In contrast to other empirical study, banking institutions, utilities, and governmental organizations are not included since their capital structure policies are fundamentally distinct from those of other business types. The results demonstrated that board size significantly and negatively affects leverage. Leverage and the number of independent directors are positively and significantly correlated.

Le and Tannous (2016) examined the relationship between shareholder's structure and gearing decision of non-financial firms registered on the VSM between 2007 and 2012. Banks, other financial institutions, and insurance companies were not included in the sample because their financial statements differed from those of other businesses. According to the study, there is conflicting information regarding how substantial ownership affects capital structure. At the 5% level of significance, both Random Effect and Fixed Effect regressions reveal a favorable link between big ownership and capital structure. While the Fixed Effect showed that large shareholding has a positive but insignificant effect on leverage ratio. The coefficient of large shareholding on the two-step system GMM is negative and insignificant. Different techniques are used during the data analysis process to address issues with unobserved heterogeneity, heteroscedasticity, and endogeneity that arise while performing regression and interpreting financial empirical results.

Safiullah (2016) investigated the consequences of board governance and shareholding structure on financing decisions of 110 companies registered on the DSE for the period 2009 to 2012. Cross-sectional regression analysis and pooled panel regression were conducted. Cross-sectional regression study revealed that board independence has a negative impact on debt financing, which is directly contrary to corporate governance principles. Independent directors play a smaller role in family-owned and -managed corporations, and they are frequently chosen from among the family. The findings also showed a positive relationship between firm size and capital structure for the entire sample period except 2010. It shows that the debt ratio decreases as firm size increases. Firm size plays a crucial role in choosing the gearing level where small firms are more likely to finance internally (from retained earnings) and have higher debt ratios as their size grows. Due to their more well-diversified portfolios, large size companies often

have a lower default probability. It makes creditor acceptability and credit ratings higher, facilitating simpler access to financing at a lower rate. Similarly, the findings of pooled panel regression analysis show that there is no significant relationship between outside directors and gearing decisions. The findings demonstrate that the choice of capital structure is unaffected by profitability. Similar results are observed in cross sectional and pooled panel regression analysis, which strengthens the study's validity. The size and independence of the board had no statistically significant effect on the firms' choice of funding.

Bulathsinhalage and Pathirawasam (2017) used secondary data of 138 CSE listed companies, excluding banking companies and financial institutions for the year 2009 to 2013. Multiple regression analysis and paired sample t-tests were applied in this study. The results demonstrated that the board size has no appreciable impact on the debt ratio. The percentage of non-executive directors and leverage were found to be positively correlated.

The CSE in Sri Lanka has 38 listed firms in the hotel and manufacturing sectors. From 2011 to 2015, Kulathunga et al. (2017) looked at the relationship between gearing level and shareholding structure of these companies. Each company's audited annual report served as the source of the data, which were then collected and subjected to descriptive statistics and regression analysis. Fixed effect and GLS models for regression analysis were used. The findings demonstrated that ownership concentration significantly improves capital structure. The capital structure is inversely correlated with the control variable tangibility.

Naseem et al. (2017) investigated the effect of institutional management on gearing level of 40 non-financial sector companies registered in PSE for the period 2009 to 2013. The data was collected from annual reports of companies and State Bank of Pakistan’s publications. The results revealed that, under the assumptions of fixed effect and random effect, respectively, number of directors on the board had a substantial impact at the 1% and 5% level of significance on gearing level.

Paramanantham et al. (2018) examined the effect of shareholding concentration on debt level of 88 organizations for the period 2011 to 2015. OLS and fixed-effect panel

methods were used for data analysis. The outcome revealed that shareholder concentration with largest shareholding is significantly but negatively related with debt structure. There is significant negative association between concentrated ownership with five largest shareholders and debt structure.

Ahmad et al.(2018) studied the effect of shareholding structure and institutional management on the capital structure of 56 Pakistani firms registered at KSE 100 index between 2011 and 2014. GLS regression is used to investigate the impact of shareholding structure and board structure on gearing level. They found that number of directors on the board is significantly positively related to gearing level suggesting that big firms with large number of directors on the board is likely to take debt on favorable terms. Board independence is positively related to leverage indicating that if board of directors comprises of a greater number of outside directors, the leverage ratio of the company will be high. The lenders consider firms with more numbers of outside directors credible making it convenient for the company to take loan from external sources. The findings showed that outside directors are major component of board structure.

Memon et al. (2019) investigated the effect of corporate governance on leverage using GLM regression of all A-shares issuing non-financial companies listed on Shenzhen and Shanghai Stock Exchanges. The data was extracted from CSMAR for the period 2003 to 2017. The sample is divided into SOEs and NSOEs. The results showed that there is a positive relationship of board size with firm leverage, but this positive relationship is statistically insignificant in the case of NSOEs. Firms with large number of directors on the board adopt a higher leverage policy to raise the worth of the firm as the cost of debt declines. The presence of independent directors is negatively connected with firm leverage, but this negative relationship is not statistically significant in the case of NSOEs.

For the years 2013 to 2017, Meah (2019) looked into how board structure issues affected the gearing level of 40 manufacturing companies listed on the DSE. The research used pooled OLS regression model. To define corporate governance factors, descriptive statistics is computed. Additionally, Partial Correlation matrix is applied to reveal the specific connections between the variables. The study also makes an estimate

of the VIF to examine the multicollinearity issue. Heteroskedasticity is also addressed using the Breusch-Pagan test. The findings demonstrated a strong inverse link between board size and gearing ratio.

Murtaza and Azam (2019) measured the influence of shareholding concentration on gearing level of 26 firms registered in the chemical sector of KSE of Pakistan for the period 2012 to 2017. Pooled Ordinary Least Squares regression was used for data analysis. The results showed a strong positive correlation between shareholding structure and gearing ratio. The agency issue between shareholders and managers is resolved by shareholding concentration. Normally, shareholders go for debt financing than financing by equity. Due to the increased amount of leverage, the larger shareholder actively controls management. Leverage ratio (short-term) have a statistically significant negative connection with ROA. The findings are in line with the pecking order theory, which shows that when profits are strong, businesses tend to concentrate on internal sources of funding. However, profitability has a positive and significant relationship with long term debt ratio. Tangibility has statistical and negative relationship with short term debt ratio and total debt ratio. Firms with higher tangibility tends to have lower firm performance. Chemical firms spend a lot money on fixed assets which do not enhance the performance if they do not use the assets properly. However, there is a substantial positive correlation between tangibility and long-term debt ratio, showing that tangibility may be helpful in lowering the chemical firm's default risk. There is significant positive relation of firm size with capital structure. Larger firms can afford high debt. Larger firms are more diversified and have fewer chances of bankruptcy.

Table 2.1

Summary of Empirical Literature

S.N.	Researchers and Date	Major Findings
1	Yermack (1996)	The study found inverse relation between board size and firm value suggesting that lesser number of directors are more effective in monitoring the management consequently delivering better financial performance.

2	Berger et al. (1997)	The study found a substantial, inverse relationship between capital structure and board size. Larger boards of directors pressurize management to seek out lower debt in order to improve efficacy.
3	Wiwattanakantang (1999)	Board size and leverage are adversely correlated in this study, however the correlation is statistically negligible.
4	Wen et al. (2002)	The study results showed that firms have lower leverage when the board of directors is small. Board size and leverage have a positive correlation, but the relation is statistically insignificant. When the number of directors increases, it is harder to come to a consensus on decisions which may result in weaker corporate governance.
5	Short et al. (2002)	The results indicated that leverage is negatively related to ownership by large external holders. The presence of large external shareholders reduces the requirement for high level of debt to be used as a means of ensuring that management do not consume excess benefits.
6	Brailsford et al. (2002)	The study provided proof that the allocation of equity ownership among large shareholders has statistically significant positive relationship with leverage. Large shareholders have greater ability as well as incentives to monitor management.
7	Anderson et al. (2004)	This study discovered a negative correlation between board size and financing costs. A larger board leads in a cheaper cost of debt, which encourages the use of additional debt.
8	Kyereboah-Coleman and Biekpe (2006)	The study revealed that firms with larger board sizes employ more debt irrespective of the maturity period in order to raise the value of the firm.

9	Abor (2007)	According to the study, there is a strong positive correlation between board size and leverage. Additionally, the results show that board composition and leverage have a positive relationship.
10	Aljifri and Moustafa (2007)	The results revealed that board size have negative impact, though insignificant, on firm performance.
11	Bokpin and Arko (2009)	The study reported a between board big connection between capital and board size. However, there is insignificant relationship with other variables.
12	Butt and Hasan (2009)	The study conducted by the author examined relationship between corporate governance, ownership structure and capital structure and found insignificant relationship between board size and leverage ratio suggesting larger board may exert pressure on managers to enhance firm performance.
13	Saad (2010)	The results of the study revealed a strong correlation between the board's size and the company's financial structure.
14	G.C. and Adhikari-Rijal (2010)	The empirical results showed that board size and leverage have a bad and statistically insignificant connection. Firms with more directors can persuade the management to adopt lower leverage to reduce the exposure to financial risk. Similarly, the number of outside directors on the board has negative relationship with leverage.
15	Sheikh and Wang (2012)	The study revealed that board size is positively related with leverage ratio which is consistent with the resource dependence theory and suggests that larger boards are better able to acquire money from outside sources to increase the firm's value.
16	Hussainey and Aljifri (2012)	Board size has little impact on capital structure choices.

17	Ahmadpour et al. (2012)	The results showed a correlation between board size and capital structure that is favorable. However, there was no discernible connection between board independence and capital structure.
18	Wellalage and Locke (2012)	The result of the study showed that presence of independent directors is negatively related with leverage. Furthermore, the findings showed that ownership concentration has no significant impact on determining Sri Lankan firms' leverage. The results also showed that board size has no impact on leverage ratio.
19	Heng et al. (2012)	The study showed that board size and capital structure have a statistically significant inverse relationship. Significant positive relationship was found between independent directors and capital structure of the firm.
20	Boroujeni et al. (2013)	The corporate governance measures, board size and board independence, have positive and negative effect on capital structure respectively.
21	Ganguli (2013)	The results showed that leverage is positively related to concentrated shareholding.
22	Agyei and Owusu (2014)	From the findings, it is evident that board size is significantly positively correlated with leverage ratio. The presence of independent directors on the board has significant impact on leverage.
23	Santos et al. (2014)	The findings confirmed a conflict between ownership concentration and leverage. Lower debt levels are a direct result of greater ownership concentration in the hands of the largest shareholder.
24	Masnoon and Rauf (2014)	The study reported that board size is positively related with leverage and is statistically significant indicating that it is easier to generate outside funds for firms with larger board size as banks consider firms with large board reliable, safe and secure. Board composition is

		statistically insignificant and negatively related to leverage ratio. Ownership concentration has negative but statistically significant relationship with leverage ratio.
25	Farooq (2015)	The findings indicated that companies with a higher degree of ownership concentration typically had low debt ratios.
26	Hermassi et al. (2016)	The results demonstrated that the size of the board and the proportion of outside directors on the board have no discernible impact on the debt of Canadian companies.
27	Shafana (2016)	The study revealed that board size and board independence have no significant impact on capital structure decision.
28	Granado-Peiro and Lopez-Gracia (2016)	The findings showed that board size has a negative and significant effect on leverage whereas the number of independent directors has a positive and significant relationship with leverage.
29	Le and Tannous (2016)	The study found that large ownership has a positive but insignificant effect on leverage ratio under Fixed Effects regression method but negative and insignificant effect under Generalized Method of Moments.
30	Safiullah (2016)	The study revealed that there is statistically insignificant impact of board size and board independence on the financing decision of the firms in both cross-sectional and pooled panel regression analysis.
31	Bulathsinhalage and Pathirawasam (2017)	The findings showed that board size does not significantly affect the leverage ratio. Leverage and the percentage of non-executive directors were found to be positively correlated

32	Kulathunga et al. (2017)	The results exhibited that shareholding concentration has a significant positive effect on capital structure.
33	Naseem et al. (2017)	The study showed that the capital structure is positively but insignificantly impacted by board size. However, under the assumptions of fixed effect and random effect, respectively, substantial influence was observed at 1% and 5% level of significance.
34	Paramanantham et al. (2018)	The findings demonstrated a strong but adverse relationship between debt structure and ownership concentration with the biggest shareholding.
35	Ahmad et al. (2018)	According to the study, board size is strongly positively correlated with leverage, which suggests that big businesses with enormous assets and big boards typically take on debt with advantageous conditions. Leverage and board independence have a good relationship.
36	Memon et al. (2019)	The findings showed that there is a positive relationship of board size with firm leverage, but this relationship is statistically insignificant in the case of NSOEs. The presence of independent directors on the board is negatively associated with firm leverage, but this negative relationship is statistically insignificant in the case of NSOEs.
37	Meah (2019)	The results showed that there is strong inverse link between board size and leverage ratio.
38	Vijayakumaran and Vijayakumaran (2019)	The study revealed that there is no significant relationship between board structure variables (board size and independent directors) and leverage ratios.
39	Murtaza and Azam (2019)	The results showed a strong positive correlation between ownership structure and capital structure.

2.3 Research Gap and Theoretical Framework

Managers frequently struggle to choose the best capital structure, which is regarded as one of the crucial corporate financial decisions. There are several theories that have been put forth in relation to this long-discussed matter. Given the abundance of information surrounding this difficult problem, no explanation can be regarded as being definitive. The necessity for the best corporate governance procedures has made it more necessary than ever before to identify an ideal capital structure.

Review of the relevant empirical evidences identified the corporate governance factors that affects the leverage decisions of non-financial companies. The influence of corporate governance on financing decisions of Nepalese listed non-financial companies has only been the concern of a small number of research. Majority of the research have been conducted on board structure and capital structure of financial institutions in Nepal. The present study has therefore attempted to fill this gap to the extent possible by including non-financial companies in the sample and not financial institutions.

There aren't many empirical studies that explore the relationship between corporate governance and the funding decisions made by non-financial enterprises in Nepal, despite the growing awareness of these concerns. Therefore, it is extremely important to research the corporate governance traits and capital structure choices of listed non-financial companies in Nepal. The study looks at how the adoption of excellent corporate governance practices may impact the capital structure of listed non-financial companies in Nepal. There is hardly any research done in Nepal putting emphasis in this area.

The theoretical framework of this study is based upon three different types of variables, i.e., dependent variables, independent variables and the control variables on the basis of previous empirical and theoretical studies. In this study, ownership concentration, board size and board composition are taken as independent variables. Dependent variable taken is debt-equity ratio of the companies. The variables that influence the relationship between the dependent and independent variables are control variables and, in this context, the control variables are age of the firm, size of the firm, ROA, tangibility and liquidity.

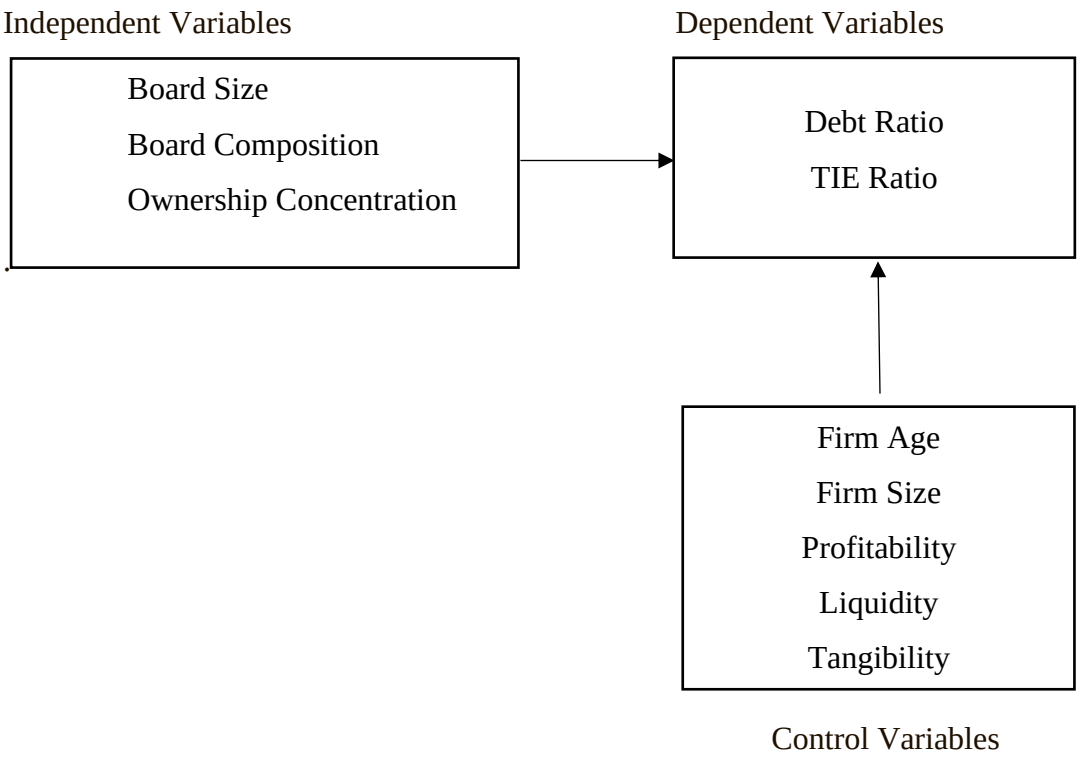

Figure 2.1. Theoretical Framework. Bajagai et al. (2019)

2.4 Variables of the Study

Independent Variables

The board size, board composition, and ownership concentration are the three independent variables employed in this study to model corporate governance.

Board Size

A crucial element of board structure is board size, which is used in this study as an explanatory variable. It is described as the total number of board members.

Board Composition

The total number of outside directors on the board is referred to as the board composition. It is determined by dividing the number of independent directors by the total board members.

Ownership Concentration

The ratio of the largest shareholder's shares to all of the company's outstanding shares is used to calculate ownership concentration.

Dependent Variables

Dependent variables of the study are debt ratio and TIE ratio which measures the leverage of the companies.

Debt Ratio

Debt Ratio, one of the measures of leverage, is defined as the ratio of total debt to total assets.

TIE Ratio

Times Interest Earned ratio is the second measure of leverage which is defined as the ratio of EBIT to interest expense.

Control Variables

This study comprises of various control variables while analyzing the relationship between corporate governance and leverage that help to control for the variation in the firm characteristics. Firm's characteristics, such as firm age, firm size, profitability, liquidity and tangibility have great influence over the leverage decisions of the firms. Therefore, the study incorporates control variables to help prevent problems connected to firm individual characteristics.

Firm Age

It is described and measured as the number of years since the incorporation of a company.

Firm Size

Firm size is measured as the natural logarithm of total assets of the company.

Profitability

Profitability is measured by ROA which is defined as the ratio of net profit after tax to total assets of the company.

Liquidity

Liquidity is measured by current ratio which is defined as the ratio of current assets to current liabilities.

Tangibility

Tangibility is measured as the ratio of fixed assets total assets.

Table 2.2

The Variable Notation

	Variables	Notations
Independent Variables	Board Size	BS
	Board Composition	BC
	Ownership Concentration	OC
Dependent Variables	Debt Ratio	DR
	TIE Ratio	TIE
Control Variables	Firm Size	FS
	Firm Age	FA
	Return on Assets	ROA
	Current Ratio	CR
	Tangibility	T

CHAPTER III
RESEARCH METHODOLOGY

This chapter highlights the research methodology used for the study. This chapter presents all the necessary steps that have been followed throughout the research work in order to achieve and accomplish the stated objective of the study. This chapter focuses on the framework of the research design, sample selection and size, hypothesis, data collection procedure, data sources and data analysis.

3.1 Research Design

This study is quantitative in nature and has adopted descriptive and causal comparative research design. The study examined the effect of board structure on leverage decisions of non-financial companies listed on NEPSE. This research aims to obtain information to describe the past phenomena. It facilitates to answer the what, when, where and how questions regarding the research problem. The finding of this research was based upon the secondary data that are published by non-financial companies listed in NEPSE. The data had been collected from audited annual reports published by non-financial companies listed in NEPSE and visit to the companies. The findings is totally based on the data and facts provided and published by the companies.

3.2 Population and Sample

Population of the research is NEPSE listed non-financial companies. There are 59 non-financial companies listed on NEPSE. Out of them, 30 non-financial companies constitute the sample of the study. Data are collected for these 30 companies for the year 2019 to 2020 and total number of observations is 30. The sample is extracted from manufacturing and processing, hotels, hydropower and trading sectors. The companies categorized as others by NEPSE has not been considered in this sample. Based on the accessibility of published annual reports, convenience sampling is used to choose the sample.

3.3 Instrumentation

The study is based on secondary source of data and were gathered from annual reports and website of the non-financial companies. The annual reports were collected from

website of the companies and those which didn't have website or had website but not updated, the annual reports were collected by visiting the companies. In this research, the major tools used as instrument for secondary data are annual reports and website of the companies.

3.4 Data Collection Procedure

The quantitative study was conducted in this research. The research methodology adopted was basically based on secondary data for all variables. All the financial data and ratios were collected from annual reports and information provided on the website of the company.

3.5 Methods of Analysis

After completion of data collection, all information were gathered, arranged and stored in Microsoft Excel and then coded to SPSS software for data analysis. This section deals with statistical models used for the purpose of analysis of secondary data.

For presentation of data, several tools like tables and figures were used. For descriptive statistical data, central tendency measures and standard deviation were used which explain the characteristics of sample companies. For inferential data hypothesis testing, correlation and regression analysis were used. The correlation analysis is used to quantify the relationship between independent and dependent variables, including its strength and direction. Regression analysis is used to determine how much an independent variable has an impact on a dependent variable.

Various tools were used to draw inferences from collected data namely:

- Descriptive Analysis
- Correlation
- Regression Analysis

CHAPTER IV
ANALYSIS AND RESULTS

This chapter contains analysis, discussion and interpretation of the results based on collected data. This chapter aims to analyze and examine the effect of board strucutre measures on leverage decisions of non-financial companies registererd in Nepal Stock Exchange. Different kind of data and ratios of the selected 30 non-financial companies have been collected and compiled for the purpose of the study. Then the data are tabulated, analyzed and interpreted. Statistical analysis have been done and presented in tables and figures to make the study and the results of the study clear and understandable. Various hypotheses that were developed during the study are tested and the results whether the hypotheses are accepted or rejected are summarized. This chapter provides systematic presentation and analysis of secondary data by using statistical techniques such as descriptive statistics, correlation and regression analysis.

4.1 Descriptive Statistics

The dependent and independent research variables' descriptive statistics are shown in this section. The dependent variables used in the study are leverage decisions explained by Debt ratio and Times Interest Earned (TIE) ratio while the independent variables are ownership concentration, number of directors and number of outside directors. The control variables are firm size, firm age, Return on Assets (ROA), Current ratio and tangibility.

Table 4.1

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation
Ownership Concentration	30	1.02	80	29.41	21.22
Board Size	30	3	13	6.8	2.18
Board Composition	30	0	20	13.21	5.91
Debt Ratio	30	0	0.79	0.36	0.27
TIE Ratio	30	-741.89	22.49	-22.55	135.96
Firm Size	30	15.22	25.08	21.52	1.67
Firm Age	30	7	58	22.4	13.49
ROA	30	-6.01	11.03	2.62	4.24
Current Ratio	30	0.13	10.83	1.96	2.24
Tangibility	30	0	0.99	0.43	0.39

The mean, standard deviation, minimum, and maximum values for each variable in the sample data set are shown in Table 4.1. The sample exhibits a wide range of variance, as shown by the minimum and maximum values. According to the above table, there are 30 non-financial companies whose data was obtained for the fiscal year 2019/20. These businesses' debt ratio is dispersed with a mean of 0.36 and an SD of 0.27. This shows that on an average, 36% of the companies' total assets are financed by debt and there is 27% variation in the debt ratio of the companies. The average value of Times Interest Earned (TIE) ratio is -22.55 with standard deviation of 135.96. The negative TIE ratio suggests that the company is reporting loss and there is high deviation in the TIE ratio of the selected companies. The average value of ownership concentration (those who own 5 percent or more of the shares) is 29.41% and standard deviation is 21.22. The mean size of the board in Nepalese listed non-financial companies is 6.8 with maximum and minimum board size of 13 and 3 members respectively whereas the standard deviation is 2.18. Independent directors constitute 13.21% of boards on an average which is significantly low.

In addition to above corporate governance variables and measures of leverage, the study employs control variables. The mean value of firm size, firm age, ROA, current ratio and tangibility is 21.52, 22.40, 2.62%, 1.96 and 0.43 respectively. ROA is very low on an average. Average current ratio is 1.96 which is considered healthy and measures the capability of the company to meet its current liabilities that are due within a year i.e. the company has 1.96 rupees of current assets for every 1 rupee of current liability.

4.2 Correlation Analysis

Table 4.2

Pearson Correlation Matrix

	Ownership Concentration	Board Size	Board Composition	Debt Ratio	TIE Ratio	Firm Size	Firm Age	ROA	Current Ratio	Tangibility
Ownership Concentration	1.									
Board Size	.365*	1.								
Board Composition	.11	.28	1.							
Debt Ratio	-.19	-.378*	-.01	1.						
TIE Ratio	-.1	-.520**	.18	-.13	1.					
Firm Size	.381*	.429*	.09	.08	-.395*	1.				
Firm Age	.372*	.436*	.02	-.552**	.12	.24	1.			
ROA	.3	.33	.11	-.737**	.13	-.15	.35	1.		
Current Ratio	.21	.381*	.13	-.368*	.16	.03	.23	.391*	1.	
Tangibility	-.34	-.409*	-.15	-.05	.2	-.490**	-.24	-.16	-.23	1.

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

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

Table 4.2 reports the correlation analysis of the variables used in the study. The correlation between debt ratio and ownership concentration is negative but there is insignificant relationship. Similarly, there is negative and insignificant relationship between TIE ratio and ownership concentration. Board size is negatively but significantly correlated with debt ratio and TIE ratio. The table also shows that board composition has negative and insignificant association with debt ratio but positive and insignificant relationship with TIE ratio. It is also found that control variable firm size has positive and insignificant relationship with debt ratio but negative and significant relationship with TIE ratio. There is negative and significant relationship between firm age and debt ratio while there is positive and insignificant relationship between firm age and TIE ratio. The profitability measure i.e. ROA is negatively and significantly associated with debt ratio but positively and insignificantly associated with TIE ratio. Current ratio is found to be negatively and significantly related with debt ratio. However, there is positive and insignificant relationship between current ratio and TIE ratio. Moreover, tangibility is found to be negatively and insignificantly correlated with debt ratio but positively and insignificantly correlated with TIE ratio.

4.3 Regression Analysis

This section identifies the independent variables that contribute to the outcome's variability and quantifies the contribution of independent variables to the variability of the dependent variables. This section presents the linear regression result of multiple regression model.

4.3.1 Impact of Corporate Governance Variables on Debt Ratio

The impact of each corporate governance variable on debt ratio has been presented below:

Table 4.3

Estimated Regression of Debt Ratio on Corporate Governance Variables

	Model 1 β	Model 2 β	Model 3 β	Model 4 β	Model 5 β
BS	-0.06*	-0.039	-0.014	-0.012	-0.016
BC	0.01	0.003	0.003	0.003	0.003
OC	-0.002	0.000	0.002	0.002	-0.001
FS	0.06	0.05	0.011	0.010	-0.009
FA		-0.01*	-0.007*	-0.007	-0.007*
P			-0.04***	-0.038	-0.040***
L				-.007	-0.011
T					-0.196
Adj R^2	0.13	0.29	0.58	0.57	0.63
F	2.04	3.45*	7.78***	6.45***	7.03***

Note: *p < .05, ** p<.01, ***p<.001

The Adjusted R^2 and F-statistic in the table 4.3 proves the validity of the estimated models. It shows the goodness of fit of the data. It illustates whether the linear regression equation provides a good fit to the data or not.

Model 1 is statistically insignificant as the p-value is greater than 0.05. Adjusted R^2 is 0.13 which indicates that model explains the dependent variable by 13% i.e., 13% variation in debt ratio is explained by corporate governance variables. Only board size is the better predictor of debt ratio in Model 1. Board size and ownership concentration are negatively related with debt ratio whereas board composition is positively related with debt ratio.

Model 2 is statistically significant at 5% significance level. Adjusted R^2 is 0.29 which shows that the statistical model predicts the debt ratio by 29%. In model 2, all three corporate governance variables have statistically insignificant relationship with debt ratio. Board size is negatively associated with debt ratio whereas board composition and ownership concentration are positively related with debt ratio.

The regression model 3 is statistically significant. The p- value is 0 which indicates that the model is a good fit of the data. Adjusted R^2 is 0.58 which represents that 58% variation in the debt ratio is explained by the independent variables board size, board composition and ownership concentration inferring that the model is effective enough

to determine the relationship. R-square is always between 0% and 100%. In general, higher the R-square, the better the model fits the data. All three explanatory variables have statistically insignificant relationship with the dependent variable debt ratio. Board size is negatively related with debt ratio whereas board composition and ownership concentration are positively related with debt ratio.

The regression model 4 is statistically significant. Adjusted R^2 is 0.57 which represents that 57% variation in debt ratio is explained by the board structure variables. Board size has negative relationship with the debt ratio whereas board composition and ownership concentration are positively related with debt ratio.

The regression model 5 is also statistically significant. Adjusted R^2 is 0.63 which represents that 63% variation in debt ratio is explained by the corporate governance variables. As per the model, board size and ownership concentration has negative relationship with debt ratio whereas board composition has positive relationship with debt ratio

4.3.2 Impact of Corporate Governance Variables on TIE ratio

The impact of each corporate governance variable on TIE ratio has been presented below:

Table 4.4

Estimated Regression of TIE Ratio on Corporate Governance Variables

	Model 1 β	Model 2 β	Model 3 β	Model 4 β	Model 5 β
BS	-35.56**	-47.04***	-50.88***	-57.00***	-56.86***
BC	7.904*	9.18**	9.102**	8.96**	8.99**
OC	1.04	0.27	-0.04	-0.16	-0.15
FS	-19.68	-19.11	-12.48	-10.27	-9.54
FA		4.85**	4.47**	4.45**	4.45**
P			5.96	3.28	3.36
L				19.69*	19.84*
T					7.32
Adj R^2	0.35	0.53	0.54	0.62	0.61
F	4.87**	7.52***	6.63***	7.88***	6.52***

Note: *p < .05, ** p<.01, ***p<.001

Model 1 is statistically significant at 1% level of significance. Adjusted R^2 is 0.35 which indicates that model explains the dependent variable by 35% i.e., 35% variation in TIE ratio is explained by corporate governance variables. Board size and board composition are the better predictors of TIE ratio in Model 1. Board size is negatively related with TIE ratio whereas board composition and ownership concentration are positively related with TIE ratio.

Model 2 is also statistically significant which shows the goodness of fit of the regression equation. Adjusted R^2 is 0.53 which shows that the statistical model predicts the TIE ratio by 53%. In model 2, board size and board composition have statistically significant relationship with TIE ratio whereas there is statistically insignificant relationship between ownership concentration and TIE ratio. Board size is negatively associated with TIE ratio whereas board composition and ownership concentration are positively related with TIE ratio.

The regression model 3 is statistically significant. The p- value is 0 which indicates that the model is a good fit of the data. Adjusted R^2 is 0.54 which represents that 54% variation in the TIE ratio is explained by the independent variables board size, board composition and ownership concentration inferring that the model is effective enough to determine the relationship. R-square is always between 0% and 100%. In general,

higher the R-square, the better the model fits the data. Board size and board composition have statistically significant relationship with the dependent variable TIE ratio whereas ownership concentration has statistically insignificant relationship with TIE ratio. Board size and ownership concentration are negatively related with TIE ratio whereas board composition is positively related with TIE ratio.

The regression model 4 is statistically significant. Adjusted R^2 is 0.62 which represents that 62% variation in debt ratio is explained by the corporate governance variables. Board size and board composition have statistically significant relationship with TIE ratio. Board size and ownership concentration have negative relationship with the TIE ratio whereas board composition is positively related with TIE ratio.

The regression model 5 is also statistically significant. Adjusted R^2 is 0.61 which represents that 61% variation in TIE ratio is explained by the corporate governance variables. Board size and board composition have statistically significant relationship TIE ratio. Board size and ownership concentration have negative relationship with TIE ratio whereas board composition has positive relationship with TIE ratio.

Table 4.5

Summary of Hypotheses Test Result

Hypotheses	**Results**
$H_{1.a}$ Board size will have positive relationship with debt ratio.	Rejected
$H_{1.b}$ Board size will have positive relationship with TIE ratio.	Rejected
$H_{2.a}$ Board composition will have positive relationship with debt ratio.	Rejected
$H_{2.b}$ Board composition will have positive relationship with TIE ratio.	Accepted
$H_{3.a}$ Ownership concentration will have positive relationship with debt ratio.	Rejected
$H_{3.b}$ Ownership concentration will have positive relationship with TIE ratio.	Rejected

4.4 Major Findings of the Study

The main aim of this study is to analyze the impact of corporate governance variables on leverage decisions of Nepalese listed non-financial companies. This section

discusses the general result obtained via descriptive analysis, correlation analysis and linear regression model based on the literature review. The following are the major findings of the study:

i. The results generated from descriptive analysis showed that there is high variation in the minimum and maximum values of variables. The mean value of debt ratio of these companies is 0.36 and standard deviation of 0.27. This shows that 36% of the companies' assets are financed by debt and there is 27% variation in the debt ratio of these companies. The mean value of TIE ratio is negative which shows the company with highest variation is reporting loss. The average value of ownership concentration (those who own 5 percent or more of the shares) is 29.41% and standard deviation is 21.22. The average size of the board in Nepalese listed non-financial companies is 6.8 with largest board of 13 members and minimum board size of 3 whereas the standard deviation is 2.18. Independent directors constitute 13.21% of boards on an average which is significantly low.

ii. The results of correlation shows that association between debt ratio and ownership concentration is negative but there is insignificant relationship. Similarly, there is negative and insignificant relationship between TIE ratio and ownership concentration. Board size is negatively but significantly correlated with debt ratio and TIE ratio. The table also shows that board composition has negative and insignificant association with debt ratio but positive and insignificant relationship with TIE ratio.

iii. The regression model 1 as generated in Table 4.3 shows the estimated results of effect of corporate governance variables on debt ratio when only controlled for firm size. Rest of the four regression models when conducted stepwise regression by controlling the variables firm size, firm age, ROA, current ratio and tangibility show insignificant results. In model 1, the board size is significantly negatively related with debt ratio whereas board composition is insignificantly but positively related with debt ratio. However, ownership concentration is insignificantly but negatively related with TIE ratio.

iv. The regression analysis in model 5 of Table 4.4 with TIE as dependent variable shows that the two of the corporate governance variables board size and board composition have significant relationship with TIE ratio when controlled for all

the five control variables. However, there is no significant impact of ownership concentration on TIE ratio.

CHAPTER V
DISCUSSION, CONCLUSION AND RECOMMENDATION

This chapter summarizes the research process and results of the study. The entire study is summarized in three sections. The first section includes discussion of the study. The second section includes the conclusion of the study derived from the findings and the third section includes the recommendation based on the findings of the research.

5.1 Discussion

The study empirically examines the relationship between corporate governance and leverage of Nepalese listed non-financial companies for the period 2019-20. Non-financial companies include hotels, hydropower companies, manufacturing and trading companies. The sectors categorized as 'others' by NEPSE has been excluded from the sample. 30 non-financial companies have been taken as sample from the population of 59 companies. Stepwise regression analysis is performed in order to evaluate the impact of corporate governance variables on leverage. Two measures of leverage have been taken into consideration that are debt ratio and TIE ratio.

Based on regression results, there is significant negative impact of board size on the first measure of leverage (Debt ratio). Board size has statistically significant negative relation with debt ratio which suggests that larger boards pursue lower leverage to reduce the exposure to financial risk. The result is also consistent with previous findings of Wiwattanakantang (1999) and Wen et al. (2002). Our finding that independent directors do not affect leverage decisions is consistent with findings of Vijayakumaran & Vijayakumaran (2019). Independent directors are added to the board just to meet the legal and regulatory requirement. Similarly, shareholders with concentrated ownership have no impact on the debt ratio of the firm.

Board size and board composition have significant impact on the second measure of leverage (TIE ratio) which is consistent with the findings of Abor (2007); Kyereboah-Coleman & Biekpe (2006). Ownership concentration has no significant impact on second measure of leverage which is in contrast with the findings of Paramanantham et al. (2018).

Board composition has significant positive impact on TIE ratio which fully supports the hypothesis developed. It implies that businesses with a higher percentage of independent members on the board may find it simpler to obtain loans and so follow a high debt policy. The majority of boards in Nepal do not meet any of the requirements that go along with the notion of independent monitoring because of the relationship-based structure in place there. Although there is a noticeable difference between full-time and independent directors and there is a recent business ordinance that requires that independent directors be appointed, there is no clear and appropriate legal definition of independence. In an attempt to maintain well-balanced independent boards, the company ordinance has made it mandatory for the companies to appoint independent directors. Moreover, Family members or nominees from the government or institutional shareholders make up the independent directors. People in positions of prominence frequently hold multiple board positions at once.

Other hypotheses developed are not supported or partially supported. This may be due to low sample size and cross-sectional data.

5.2 Conclusion

The study attempts to examine the effect of corporate governance on the leverage decisions of non-financial companies listed in NEPSE. The study is based on secondary data collected from 30 non-financial companies listed in NEPSE for the period 2019-20. The study concludes that board size has significant effect on the leverage as measured by debt ratio of non-financial companies listed in NEPSE. However, board composition and ownership concentration do not significantly affect the debt ratio.

The study has identified that except ownership concentration, board size and board composition have significant effect on the leverage of the companies as measured by TIE ratio. The study reported having large number of directors on the board significantly affect the ability of the companies to pay its debt obligations from the earnings of the companies. Similarly having more independent directors on the board significantly affects the TIE ratio. However, ownership concentration does not have significant effect on the leverage of the companies as measured by TIE ratio.

5.3 Implications

There has been very limited research on the corporate governance mechanisms and leverage decisions on non-financial companies in Nepal. The study may be useful to conduct further research in this field as there has not been full awareness of corporate governance practices and its effect on the leverage decisions as well as performance of the company. The study provides useful references to future researchers and scholars.

This research is purely academic research, so only 30 non-financial companies are taken as sample due to unavailability of data. The researcher has difficulty collecting the data. It is recommended to disclose the board structure and ownership structure clearly in the annual reports and publish the same in the website of the companies so that it would be convenient for future researchers to conduct further research in this field. Only three corporate governance measures have been taken as independent variables due to unavailability of data of other corporate governance variables like board meetings, CEO compensation, CEO duality, etc. Similarly, this research is based on cross -sectional data. Only one fiscal year has been taken into consideration for data collection due to data constraints. The number of observations is low which affects the overall result of the research. Panel data provides better results than cross sectional data. Therefore, it is recommended to conduct analysis on panel data for future research as the sample size is few. The results will be reliable if future researchers can take the changes in board structure over the period. Finally, this research generates a scope for several other researchers who want to do research in corporate governance in Nepal.

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Appendix

SN	Listed Non-Financial Companies	Ownership Concentration	Board Size	Board Composition	Debt Ratio	TIE Ratio	Firm Size	Firm Age	ROA	Current Ratio	Tangibility
1	Oriental Hotels Ltd	34.012%	7	14.286%	0.198	2.587	21.926	28	2.009%	2.483	0.700
2	Soaltee Hotel Ltd	50.000%	8	12.500%	0.002	0.842	21.645	55	4.458%	1.334	0.570
3	Taragaon Regency Hotel Ltd	26.080%	11	18.182%	0.013	15.016	21.946	28	4.984%	1.866	0.507
4	Barun Hydropower Co. Ltd.	10.624%	7	14.286%	0.460	0.213	20.095	18	1.203%	2.805	0.885
5	Butwal Power Company Ltd	56.280%	10	10.000%	0.031	22.497	22.786	56	9.296%	6.465	0.040
6	Chhyangdi Hydropower Ltd.	6.111%	6	16.667%	0.646	0.583	20.698	14	1.581%	0.623	0.425
7	Chilime Hydropower Company Ltd	51.000%	11	18.182%	0.000	0.000	23.076	26	7.089%	10.833	0.018
8	Himalaya Urja Bikas Company Ltd	5.853%	7	14.286%	0.652	0.000	21.872	22	0.145%	0.844	0.020
9	Himalayan Power Partner Ltd.	35.700%	7	14.286%	0.691	0.000	22.035	17	0.000%	5.846	0.006
10	Joshi Hydropower Development Company Ltd	1.018%	3	0.000%	0.360	-0.274	20.123	7	-3.364%	0.129	0.991
11	Kalika power Company Ltd	41.996%	7	14.286%	0.436	0.910	20.957	14	4.049%	0.837	0.966
12	Mountain Hydro Nepal Ltd	23.836%	7	14.286%	0.703	-0.302	22.279	16	-2.373%	0.361	0.004
13	National Hydro Power Company Ltd	5.441%	6	16.667%	0.072	8.327	20.831	22	4.703%	2.272	0.881
14	Nepal Hydro Developers Ltd.	16.875%	4	0.000%	0.529	0.890	20.187	15	4.886%	1.900	0.002
15	Ngadi Group Power Ltd.	9.810%	7	14.286%	0.309	1.963	20.656	16	6.271%	1.116	0.749
16	Panchakanya Mai Hydropower Ltd	24.773%	4	0.000%	0.663	0.077	21.868	19	-1.752%	0.202	0.971
17	Panchthar Power Compant Ltd	18.237%	5	20.000%	0.668	0.505	21.569	13	-6.014%	1.594	0.998
18	Radhi Bidyut Company Ltd	63.496%	6	16.667%	0.294	2.074	20.701	18	7.425%	1.670	0.511
19	Rasuwagadhi Hydropower Company Ltd	32.790%	6	16.667%	0.482	-1.808	23.260	10	-0.578%	0.260	0.012
20	Sanjen Jalavidhyut Company Ltd	39.360%	6	16.667%	0.559	-2.088	22.758	11	-0.469%	0.813	0.000
21	Synergy Power Development Ltd.	16.240%	5	20.000%	0.575	1.533	21.034	15	1.174%	2.575	0.027
22	Union Hydropower Ltd	22.793%	4	0.000%	0.219	0.581	20.526	15	1.372%	2.834	0.902
23	United Modi Hydropower Ltd.	7.336%	7	14.286%	0.000	0.000	15.224	14	7.710%	2.803	0.721
24	Upper Tamakoshi Hydropower Ltd	41.000%	13	7.692%	0.517	-741.897	25.084	15	0.197%	0.241	0.000
25	United Idi-Mardi and R.B Hydropower Ltd	23.000%	5	20.000%	0.796	-0.437	21.073	12	-2.918%	0.250	0.978
26	Bottlers Nepal (Terai) Ltd	76.160%	7	14.286%	0.474	0.028	22.842	34	0.068%	0.542	0.007
27	Nepal Lube Oil Ltd	39.960%	7	14.286%	0.366	0.391	20.321	38	6.124%	1.438	0.252
28	Shivam Cements Ltd	10.560%	6	16.667%	0.019	11.120	23.300	18	11.033%	1.662	0.335
29	Unilever Nepal Ltd	80.000%	7	14.286%	0.000	0.000	22.038	28	9.615%	1.447	0.291
30	Salt Trading Corporation Ltd	12.000%	8	12.500%	0.001	0.136	22.913	58	0.700%	0.901	0.171