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Effect of Financial Gearing and Financial Structure on Firm's Financial Performance

Evidence from Pakistan

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Abstract:- Finance has utmost importance like blood for any company. However, better utilization of funds, resources or use of debt / equity mixture smartly, has remarkable influence on organization's financial performance. Better implementation of gearing strategy moderates the risk and improves operational efficiency as well as maximizes shareholders' wealth. The key concept is to explore how financial gearing and financial structure affect financial performance along with their link between each other by observing the 12 publicly trading textile companies registered in the PSX having time span from 2011 to 2020. The study used quantifiable approach together with multivariable regression models to analyze the assumptions. Outcomes as a whole demonstrates that when there is no downturn economically in the country, low levels of gearing inclined towards high margins of profit along with high return on equity and assets also. Those external borrowings which are an integral part of gearing should less depend but more concentrate to develop strategies internally in order to enhance the company's financial performance. This study also provide confirmation by estimating different veracities that the key components of the Pakistani textile companies to develop their operational and financial performance by using the gearing strategy might reap maintainable imminent development.

Keywords:- *Financial Structure, Gearing, Firm performance & value, Shareholder's Wealth.*

I. INTRODUCTION

The stock price of the company reflects the company's success regarding value of firm in management of its resources. If stock price increases value of the firm is also increases towards the maximization of shareholders wealth. More is the stock price in the market; more will be the firm's value (Fenty & Rafiqoh, 2021). Every organization utilizes sources of finances to support and/or to increase their sales as a result to escalate profitability as well as wealth of shareholders towards the economic growth of the country (Dr.N.S. panday & Prabhavathi,2016). In this regard financial managers are more concerned with the debt & equity level to establish optimal mixture of capital structure for their operations for maximization of earnings along with minimizing the cost of capital (debt and equity). Financial cost increases with the increase of financial gearing (Deavina & Husodo, 2021). However, investors are generally don't have awareness about the statistical value of their investment interconnected with financial gearing where profitability of the company may have adverse effect and can ultimately affect the stakeholders' earnings if invested amount is greater than the company's profitability (Afza & Hussain, 2011). Accordingly, risk is integrally associated with leverage, typically demarcated by the hostile effect on earnings of numerous uncertain discrete sources. While an organization's level of risks and its type dependent on numerous aspects for example, its volume, magnitude, complication of business activities and size etc. If companies have clear and better awareness of risks can reduce its likelihood resultantly enhance the organizational control on its market activities and thus declines the volatility of its revenues & cash-flow. (Krause & Tse, 2016).

An organization's financial structure is consisted of only equity shares called unlevered company while if financial structure of an enterprise is consisted of equity and debt called levered company (Olweny and Mamba, 2011). The proceeds of financial gearing are used to get high returns than cost of debt as well as interest expense (Cheng and Tzeng, 2010). In evaluating and directing economic industry and capital markets, the Financial Structure has utmost effective aspect. Therefore, management executives should consider increasing the size of their allocators by determining the best financial mix for their company. Now recently in valuation of performance and to enhance the value of the firm, the financial decisions with regard to growing prospects have become rational. In the year (2012 Tudose) explained the performance in ways: organizational as well as financial both are interconnected, that on the basis of variables which include returns, development, productivity along with satisfaction of the customer, the measurement of company's performance is possible.

Generally, it is considered that company performance is influenced by the use of leverage. Currently, company's businesses lean towards continually modify their financial structure with passage of time subject to variations in numerous inward and outward aspects. (Bajaj et al, 2020). Ultimately, in this research the leverage effect on financial performance of Textile Companies of Pakistan will be evaluated. The research results will support to understand the ensuing facts affecting the earnings through performance by considering choosing the type of leverage.

Conclusions will also specify the performance & gearing association of the organizations in a way to evaluate their financial necessities and to know at what level leverage should employ to have positive yields for shareholders. This research study will provide help to the organizations to evaluate their operational and financial requirements, proficiency to progress and in what way it is useful to increase returns for investors and in the end for Pakistan's economic growth.

Research Problem

Borrowings and company's own funds are the two basic financing modes. Choosing an appropriate financing is the basic requirement of the companies. Management tries to implement most suitable way to finance keeping in view the maximum benefits of shareholders. Practically, Companies are functioning in an ambiguous situation (Markovitz, 1959). That is why; companies may face variations in returns. Practically, the actual situation is much different having complications in a competitive market as compared to theory. Financing through debt is valuable in case if return on equity and levels of profits is increased (Kale, 2014). Many deliberations are still stand regarding optimum mixture of funds to progress the firm's financial performance considers reducing the risks collectively interlinked with resources of funds. Past studies explored a little with respect to financial gearing as well as financial structure impact on financial performance but did not find the influence in liquidity as well that have vital role to establish that firms utilizing financial gearing could meet their financial commitments or not. The previous studies do not demonstrate the long run impacts of inappropriate gearing levels on performance which finally hit the shareholder's wealth. Definitely, the firm's achievement is depended upon the perfect financial structure ascription. In view of the above, the research problem can be framed as per below question:

"What is the separate as well as combined impact of financial gearing and financial structure on firm's financial performance?"

Study Significance:

The study's main objective was to focus on profitability, mainly in the Pakistani capital market and to assess the impact of a mixture of costs and equities, as measured by the leverage, and company's financial performance.

1. Though several researches have investigated the relation of gearing level with financial performance, but the numerous research studies have been selected markets of developed countries and the relation in between financial structure and financial performance has been developed through tax incentives and tariffs between prices and profits using capital payments. Therefore, current research was designed to observe 3 related relations affecting financial performance: investment, financial structure and financial performance. Hence, this method was helpful to study the relation of optimum financial structure mixes and low gearing level towards the firm's financial performance.
2. Future researchers and scholars with experience of this research will quote this study and it can be referred as a base for further research and the study results on the relationship between these factors and the current economic situation of Pakistan can be used as a basis for future studies along with its relationship with other factors of capital and industrial performance.
3. Competitive power refers to the fact that strong pressure can be exerted by the other parties having market share or on the profitability in the same company. Hence, this study provides guidelines for business executives and policymakers in the company's business process that should be carefully planned before selecting funding.
4. The significance of this study stems from the current need for economic and trade capital of Pakistan. The importance of this study comes from considering three important factors - cost, equity and interest that affect corporate profits in and around the Pakistani industry.
5. This study is to expand understanding and documentation of how leverage works in the financial system based on high interest rates.
6. The current research is beneficial for listed companies because it shows the cash flow effect and investment towards financial performance.
7. Through this study, companies will also be able to comprehend the significance of retaining the best optimum financial structure to maximize market and economic benefits in Firm's value.
8. This study adds to the current knowledge about the need to leverage the company along with how to help with the company's financial performance.
9. With the knowledge of the authors, the current study discovers the path of trade relations in connection with labor as well as capital.
10. Current research investigates the magnitude in which financial structure and strong performance is based on high level of competitiveness that companies perceive first in Pakistan.
11. This study will be useful in recommending the type of business plan that is better or more appropriate should be initiated to maximize performance and industry standards.
12. Empower the management Executives like CFO or CEO of the firms to know how financial structure options to select the best capital mix ratio have influence on company's financial performance.
13. The investors will get help from this study in Pakistan to generate a portfolio in earning the highest profit and maximum financial benefits.

Contribution in the Research Studies

Former researches were primarily related to analytical subject matter or indicators which are stated in initiatives in general, the relationship between financial structure, financial gearing and financial performance has also revealed in some researches capturing only the business areas of export, tourism, mining, hotels etc. On the contrary, textile industry comprises of its particular features and remarkable differences among various markets. The final results of these researches were not grasped in the same line because of the difference between making and setting the assumptions under various circumstances.

From the review of the different studies there is still a deficiency of such type of practical research in Pakistan which can focus on determining the impact and connection between financial structure, gearing & company's financial performance in consideration of financial aspects paying special attention on that criterion which adds value to the earnings of the Textile companies. Hence, this study will help in providing solutions of the problems in researches done before and seek a revised model concerning effect of financial gearing on firm's financial performance in the form of profitability and liquidity toward the value of the firm in the end. On reviewing literature of earlier studies, there has been no research which has dispensed with this angle.

Hence, knowledge of the researcher which differentiates the study is that it brings together with financial aspects that are quite significant for the financing discipline towards both practical side as well as the applications side because financial gearing is one of the elementary columns in operational and financial decision making. This study scope has financially two-fold effect on firm's financial performance in the shape of firm's structure and financial gearing represented in this research.

Objectives of the Study

The present study tries to contract the below mentioned key objectives which are:

- To observe the effect of financial gearing and financial structure on financial performance of Pakistani companies of textile industry separately.
- To observe the financially mutual impact of gearing along with structure of capital on financial performance of Pakistani textile companies.

Research Questions

The below mentioned research questions are the part of this research study:

- Whether any relation exists in connection with financial gearing and financial structure with organization's financial performance?
- What is the combined effect of financial gearing and financial structure on organization's financial performance?

Research Hypothesis

The business model states that capital is appropriate based on how a company adjusts the value of its capital components. This can be attained by generating equilibrium concerning tax revenue and debt, and then reducing corporate costs, as well as the risk of lack of funding and financial crisis (Ayen & Oruas 2008). The business's profit margin trades against its value to maximize the company's profitability. Therefore, in such a case, the real capital would be used to pay the minimum and maximum amount.

Hypothesis

H1: Firm's financial gearing and financial Structure significantly influences the organization's financial performance.

H2: A significant relation is existed among financial gearing, financial structure and Firm's performance.

II. RESEARCH METHODOLOGY

This research study has targeted population of Pakistani textiles firms registered in PSX. In this present study, the secondary data was collected from the annual reports of 12 textile firms having time span from 2011 to 2020. Keeping in view the secondary data type e-views software is used to get best results. The current study has used balanced panel data. To grip the findings estimation techniques, (fixed and random effects and OLS technique to confirm relationship) are used Whereby Hausman's test has been applied to confirm which technique (fixed effect or random effect) is best to accept for analytical purposes.

III. LITERATURE REVIEW

Defining structure of the capital at its optimum level to add value of the firm is an argumentative subject area in the literature of finance. Many studies depict the suitability of mix structure for one company while the same is not suitable for other sectors or areas. Bhatti & Nguyen (2012) studied dire need of structure amongst financial markets. **S**ome of the following theories describe the development process of mix optimum capital structure involved leverage in the form of debt which creates fixed expense cost who eventually influence the company's performance. The base of these theories was to define the debt-Equity guidelines in a company's capital structure originated on tax and insolvency ruins also.

Theories Related to Financial Gearing and Financial Structure

In 1958 Modigliani & Miller determined the **"Irrelevancy of financial structure"** to hit firm's value called M.M. Theory (Ebaid 2009). The value of the firm is not dependent or relate to ratio of Debt and equity. A company's avg. capital cost is totally independent against its financial structure while equity is equal to its capitalization rate. In 1961 Donaldson presented **"Pecking order theory"** the firm performance or profitability stresses preference to use readily available internal funds to be spent first, followed by debt as such funds are relatively cheaper to raise fresh equity; and then if funds are still needed, firms should go for new equity as a last option. Later on, in (1999, Shyam et al) and in (2018 Zeidan et al) explored implementation of this theory in Brazilian companies. In 1932 from Berle & Means the history of stockholders or shareholder theory started but in 1962 Friedman presented "**Shareholders' theory"** called the father of this theory. He believed that it's the fundamental duty of management executives is to enhance wealth of the shareholders in any authorized manner (Danielson, Heck & Shaffer 2008). In 2000 O'Sullivan debated that shareholder depend on others to make the company's operations effective. The company should operate in the interest of shareholders towards the shareholders wealth maximization as they are the principals of the organization. Based on M & M theory, in 1973 Kraus & Litzenberger eliminated irrelevant assumptions of M & M theory where they overlooked the taxes impact or crooked evidence. In contrast Kraus presented a **"Trade-off Theory"** that "there should be comparable of same financial gearing ratios of companies of the same industry because

companies try to optimize the tax savings due to the market value of levered firms equals the market value of unlevered plus tax shield benefit subsequently eliminating the financial costs". This theory explains that a company must successfully balance components costs of financial structure in order to get optimum financial structure. The advantages of this theory to enhance the value of the firm are traded against their costs. In the year 1976 Jensen and Meckling define in their **"Agency Theory"** about the relation between firm's value and the leverage. This theory is interrelated with agency problems generates in the corporation due to clashes between shareholders and management executives or other stakeholders or clashes of benefits (Ayen & Oruas 2008). In the light of this theory the principal (shareholder/s) engross with the agent (other person/s) to execute a particular deal on behalf of them which contains to authorize decision making power to the agent. Large organizations having shareholders large in size may have more ability to lessen agency costs with respect to small organizations having shareholders small in size. The reason is that shareholders large in size have more funds and inducements to watch organization's management executives (Zerni, Kallunki & Nillsson 2010). Another theory **"Cash flow & Free Cash flow"** deals with costs of free cash flows and the way how to balance the flow of cash while debt averts management executives to continue the intentions individually, as the risk of insolvency would increase. Thus, in the light of this theory, profitability and leverage at high level would have a favorable relation. But some other research studies depicted the adverse relation between free cash flow and the debt. For instance, in the year 1995 Hart & Moore described that the debts which are long-term in nature controls the management's capability regarding to finance the investments in future. While under the "**Stakeholders' theory"** the management executives not only deliberate the shareholders but must also consider stakeholder's benefit while making the decisions (Jensen 2002). This theory emphasizes that stakeholder's interest should be take into account as they have bargaining power. More expressively, this theory describes that customer, investors, employees of the organizations and management groups are included in stakeholders. In 2004 Freeman et al., depicted that management executives must generate such relationships which can motivate the stakeholders in making the communities so that each person can take part actively in value addition of the company. Consequently, the **"Theory of Dual-Investor"** provides the solution of conflicts between both theories of shareholder and stakeholders. Schlossberger (1994) demonstrated this theory that projects of each business have two types of investors. Firstly, owners of the stock who deliver particular capital to the business project while secondly, the whole society which delivers opportunity capital. Hence, a balancing relation exists between shareholders and stakeholders to increase the value of the company. A substitute of agency theory is the **"Theory of Stewardship"**. Herberg, Mausner and Snyderman (1959), McClelland (1961) recommended that managers itself interested in disposition to attain, get gratification to effectively execute the work of challenging in nature in order to enforce obligation along with power to provide advantage to the organization. Irrespective of above said research studies which observe the theory of Stewardship, Davis, Donaldson and Schoorman (1997) demonstrated that agency theory is the base of the theory of Stewardship as a hostage approach. In 1977 Ross established this model hypothetical structure as an incentive–signaling to define the theory of company's financial structure. This theory indicates that a company having positive projections will generate new capital via financing through debt while a company having negative projections will prefer financing through equity. However, signaling theory may be used to raise the value of firm's stocks. Hence, theory of signaling expresses that management executives of the company sent signals to the investors through their financial decisions to stir the irregularities. The policy of financial infrastructure is based on these signals. While considering **"Market Timing"** theory researchers hypothesize "time" in their research study because time matters for companies to issue new equities. Basically, this theory is in comparison of both trade-off and Pecking order theories and called latest financial structure theory. Boudry, Kallberg and Liu (2010) stated that when a company's management feels that their firm is overvaluing in the market, they decide to issue new equity. It all depends on their value of the firm in the market.

Cronqvist et al. (2012) explained in **theory of Behavioural consistency** that companies' management of top level steadily act where there is need to select company's gearing. Lam et al. (2013) presented **Norm theory** about behavior (norms) of the managers in the line of environment and regarding their dealings with juniors which influence the decisions about financial structure. The latest theory related to gearing is the **theory of Bargaining** presented by Chu and Wang in (2017) explained that suppliers of the company raise their gearing in response of raised gearing by the company in order to sustain negotiation power with their substantial customers. On the contrary, when gearing raised by the customers, in response Company will reduce its' gearing level to decrease its risk of insolvency.

Review of Literature of the Factors in Selecting the Debt or Equity Option

If a company has tangible assets in large amount it uses to prefer debt capital while it has significant percentage of intangible assets, it uses to prefer equity (Harris & Raviv 1991). Myers (2001) described that still no complete theory has been developed to choose the ratio of debt / equity and have no cause or motive to suppose a comprehensive debt/equity theory to select the ratio option. Various research studies used methodologies different in nature have different outcomes along with dissimilar clarifications. Some researchers Al-Saleh, Abo Hussain and Al-Ajmi (2009) defined another factor for variation in the outcomes is to account for different situations. They explained that one situation could not be inevitably generalized or fit for other environments. Organizations have different options to choose different resources to raise their funds. Charalambakis & Garrett (2010) described in his research study that companies give preference to issue debt in case of high rates of average tax, on the contrary those companies which have probably high distress in financial point of view are unwilling to raise debt. Those companies which are making large amounts of profits and have durable position of their finance are

anticipated to raise additional debt instead of equity. Situation of the market and tax related matters effects the option in using the financial tools. By taking into account the tax shield benefits companies are often preference in using the debt option instead of to raise equity capital.

Empirical Review of Financial Structure and Performance of the Firm:

Tan and Hamid (2016) examined the relation between cost and industry performance by select an example of 41 companies listed in the agricultural sector in Malaysia for time span from 2007 to 2011. The survey results show a favorable and relevant relation between large salaries and selected Malaysian firms' performance. By selecting 136 listed companies in Abata and Migiro (2016) studied the capital impact assessment and performance of listed companies in Nigeria. Examples of 30 companies surveyed during 2005 to 2014. The results of a multi-tasking survey showed that both operating employees returning equity reduced the debt burden. Mauwa et al., (2016) used head-to-head data for firms registered on the Rwanda Stock Exchange (RSE) of Nigeria to analyze the relationship of gearing and performance. The survey results show iterations that show that all aspects of a company's performance, i.e., ROE and ROA, are in the company influencing and influencing profitability.

Performance Analysis

The performance perception has multidimensional meanings due to which it has become debatable. There are two types of performance measures like operational and financial. In accordance with Tudose (2012) the selection of alternative performance methods (financial or operational) is depended on set objectives. According to Abdul-Malik et al. (2014), financial performance factors such as increasing profits on assets, and increasing benefits of the shareholders are key factors for company performance. Market growth as well as sales growth represent performance characteristics; deliver a comprehensive description of performance. The reason is that they emphasis such factors towards financial performance. Malm & Roslund (2013), explained that performance can be measured for a company's specific department or can check as overall. This study will focus on the overall firm's performance. This research study will concentrate on comprehensive measures of performance for whole of the company keeping in view the profitability towards the enhancement of shareholders' wealth.

Profitability Analysis

Response Variables: Normally, most common response variables ROA, ROE and ROI are used to evaluate firm's efficiency in producing the profits, performance and financial health. Ehrhardt & Bringham and Ross et al. (2011) while Gitman and Zutter (2012) calculated ROA by Net annual Income to total assets and ROE with net profit to total equity while Lindow (2013) calculated ROA by taking EBIT to total assets and ROE with EBIT to total equity. Malm & Roslund (2013) explained that ROE indicates the firm's ability to find the opportunities for investments which have a substantial importance for the companies to stay competitive. Accordingly, the third response variable ROI has direct connectivity with procedures of accounting and it is easily calculated from the final accounts of the company to find the return on invested capital. Its formula in accordance with ACCA financial management study text is

$$Return\ on\ Investment\ (ROI) = \frac{EBIT}{Capital\ Employed}$$

In this formula capital employed can be calculated as:

$$Capital\ employed = Shareholders\ Equity + Long\ Term\ Liability$$
$$Capital\ employed = Total\ Assets - Short\ Term\ Liability$$

Gansuwan & Onel (2012) described that creation of value for shareholders is only valuable when a company receives return on employed capital greater than the invested capital's cost. Bender and Ward (2002) examined that if a firm increases the ROI in that case more funds will be available to reinvest capital which will cause to escalate the maintainable level of growth.

IV. DEBT ANALYSIS

External borrowings in a financial structure are called debt capital. Normally, the safest type of borrowings is the long-term debt. The reason is that firms have much time to payback the principle but just to pay the interest only (Nawaz, et al. 2011). Different organizations used the public money by depositing it in the company as debt finance. For example, companies received money as a loan from their employees, customers and shareholders without issuing shares and debentures. Companies consider that money as public deposit or loan from public. When a company decides to run its operations through external borrowings, the company runs a financial risk and calls it a payroll company. Earhardt and Bringham (2011) define financial risk as an additional benefit for shareholders result in borrows money decision. Debt has a fixed income which is typically in the interest form causes to increase risk.

Financial Gearing:

In financial structure of every business, financial gearing is the capability to smartly use its sources of fund like preference shares, shareholders equity and external borrowings to enhance its positive impacts on EBIT towards net income. Shareholders tolerate fixed charge of financial gearing with the expectation to get more future returns than its fixed cost. Financial gearing mostly used to enhance the capability of EBIT towards the improvement in EPS (Saleem, Rahman & Sultana, 2013). Financial gearing having distinction due to the interlinking with firm's financial structure along with its relation with capability keeping in view Several stakeholders' interest.

Financial Structure

Corporate financial statements have shown that not many educated people describe financial structure or resources in a narrow way, putting long-term debt into it (Graham, 1996; Devic & Krstic, 2001). However, short-term

payments as well as long-term capital to participate in capital planning also incorporated due to a number of reasons. First, Lindsay & Harwood and Rasu (2000) also found that tax rates are directly related to debt growth because long-term debt leads to higher interest rates now. Second, emerging financial institutions may offer them shorter wages and less support for large-scale conditions associated with asymmetric information and unsatisfactory sales (Demirguc-Kunt & Maksimovic, 1998). Third, in times of low interest rates, companies may incur short debts, such as bank loans, business insurance, and so on. In addition, the management role of corporate executives by lenders is becoming increasingly effective due to short-term debt (Delcoure, 2007; Fung & Goodwin, 2013). Therefore, containing of long and short-term prevention in the design of corporate headquarters is better (Omet & Mashharawe, 2003; Nikolaos et al., 2007; Joeveer, 2006; Gaud et al., 2005).

Financial Performance

Yahaya & Lamidi (2015) stated that giving the performance financially states to a company's capability to attain its objectives along with financial tasks. Kajirwa (2015) concluded that company's financial performance depends on company's assets usage to operate its financial well-being. A company can generate and increase profits based on its business performance and capabilities. Vijayalakshmi & Manoharan (2014) explained that the power of a business is the function of financial management to get money when needed from the lowest source of corporate income. Business activity refers to the efficient use of corporate resources to escalate production capacity. In case of gaining huge profits, a company is able to withstand high costs because it has a high potential to achieve financial performance from debt acquisition, which means that the profitable company adds more. Financial performance is critical to a company's economic success because of the way the company achieves its financial goals and objectives of economic growth (Xu & Wanrapee, 2014).

Financial Gearing and Financial Performance

Many clear and concise descriptions seek to describe the interaction and performance of a company. In principle, the roll-by-roll system emphasizes that companies have a system to choose from when they receive funding. The provision of funds depends on the debt and availability of this type of loan (Mukras and Mule, 2015). Raza (2013) stated that trade data show that a good financial structure can only be achieved in case of equilibrium in connection with capital's cost and the company's cost. Jafari and Moghaddam (2015) examine the need for job placement. The outcomes depicted that a positive relation exists in between the financial performance and company's investment. The study also explored that companies are more profitable which having higher capital gains as compared to companies which are less profitable.

Financial Structure and Financial Performance

The relation between performance and capital gains / profits is an ongoing topic among academic researchers. The documents state that real equity and fees are required when developing a business-to-business strategy because it is a key factor in improving a company's performance. When a company announces an increase in new shares, it gives its distributors a negative signal and as a result reduces the market share of those shares. In addition, companies with weak financial resources spend their earnings from equity only to spend with potential investors. As a result, company's profitability is affected by investment. Furthermore, the concept of "late in order" also explains that the main cost of using the right host presence can undermine a company's profitability. Numerous researches as Abor (2005), Baum, Schafer & Talavera (2006), Dwilaksono (2010), Gill, et al (2011), Shubita & Alsawalhah (2012), have shown a correlation between wage and industrial value. Companies must have an optimal financial structure as they have to strike a balance between profit or loss (Myers & Majluf, 1984). The best design of the house makes the economy more profitable by reducing the price of financial options.

Corporate Financial Structure in Developing Countries

The reporting of firm's financial structure along with its elements would be fascinating which work under the uneven circumstances of economic and political in nature and make a comparison of available literature with outcomes. Bas, Muradoğlu and Phylaktis (2009) discuss capital planning decisions for companies and emerging markets involving 25 countries from different regions. Unlike previous researches, to concentrate on small firms is the main purpose. The reason is that these small firms have vital role to more contribute in GDP as compared to large companies but they constitute a large proportion of companies in developing countries. This survey examines whether urban resource settlers reflect variances between small, medium and large enterprises, and examines whether capital settlers are same listed companies. Booth et al. (2001) examined the financial structure of companies in 10 developing countries: Malaysia, India, Turkey, Zimbabwe, Pakistan, Thailand, Mexico, Jordan, South Korea and Brazil. They ponder those decisions for investment and their impact vary from country to country and also whether the type of capital structure predicts better if the company is a citizen.

The researchers determined that models of financial structure have forecasting power in under developed and developed countries. They noted that the small companies having large tangible assets, which are paying tax and are profitable, have less debt in total apart from more debt in long term. In the end apart from ratio of market value, financial variables at least are affected by the dynamics of the country.

Empirical Literature of Pakistan

Mostly Pakistan's pragmatic research studies examined only financial structure's direct effect on performance of the firm with the help of different samples of Pakistan's industries. Tauseef et al (2015) studied the efficiency and gearing relation by taking Pakistani 95 registered firms' sample for time span from 2002 to 2008. Financial performance was measured through ROE where the capital structure is calculated with cost reduction. The results show an unrelated relationship between high returns and equity. This means that with increased leverage, the company's performance increases to its best capital level and then starts

to decline. The study also determined that the best debt level is around 56 per cent in Pakistan's textile provinces. Moreover, the company's market growth predicts a return to company size does not reflect the company's performance. Ahmad & Mohsin (2016) described financial structure effect on the firm's performance related to Pakistani cement industry by taking 18 registered firms for time span from 2009 to 2015. Performance was calculated with help of total asset's return in which debt was incurred to calculate gearing. The outcomes reflected an adverse and costly relation between debt and profit. Similarly, Uwais et al. (2016) demonstrated the capital influence on company's performance by taking 100 registered non-financial Pakistani firms having time span from 2004 to 2012. Surveys show that total debt improves the performance of all companies, such as ROA, ROE, and Tobin's Q measures and earns in long and short run. Debt settlement can make a company performance better.

Habib & others (2016) expanded the available document by analyzing the relations between gearing and performance by taking sample of 340 registered Pakistani companies having time span from2003 to 2012. This study uses SDR, LDR and TDR as predictors of change because company performance is measured by asset returns. Survey consequences reflected the adverse relation between whole financial structure and corporate performance.

There is dire need to research those effects which affect in determining the optimum financial structure regarding financial performance of the company. For professionals and academic analysts, financial structure is the key subject in corporate finance. The best ratio of debt and equity which can minimize the cost of capital along with risk of insolvency called the optimum financial structure of the company. In conjunction with this study, these studies were nominated because they are meticulously interrelated with one another and have influence in making the decisions about financial performance and financial structure.

V. FINDINGS, RESULTS ANALYSIS AND DISCUSSIONS

The purpose of overall review descriptive analysis is to test the hypothesis framed earlier for accomplishment the relation among the stated variables.

Table – 5.1 Overall Descriptive Statistics of Variables

Description	ROI	ROE	ROA	INTEREST _COVER	F_L_ RATIO	DEBT_ RATIO	DEBT_ EQUITY
Mean	0.158594	0.093929	0.041350	0.453170	-2.700814	0.555705	1.486921
Median	0.152595	0.086313	0.037580	0.408378	1.623326	0.581523	1.389633
Maximum	0.489534	0.449744	0.227475	2.965053	190.4681	0.798827	3.970837
Minimum	-0.218187	-0.427354	-0.153483	-1.779641	-969.6867	0.226485	0.292800
Std. Dev.	0.108238	0.110955	0.047972	0.473277	92.35199	0.135689	0.831763
Skewness	0.466969	-0.1317	0.489121	0.405532	-9.548539	-0.274402	0.968667
Kurtosis	4.617769	7.047338	6.613201	13.52683	102.1168	2.146762	3.668700
Jarque-Bera	17.44708	82.25161	70.06090	557.3601	50944.15	5.146002	21.00213
Probability	0.000163	0.000000	0.000000	0.000000	0.000000	0.076306	0.000028
Sum	19.03124	11.27149	4.962039	54.38039	-324.0977	66.68456	178.4305
Sum Sq. Dev.	1.394128	1.465009	0.273852	26.65498	1014938.	2.190971	82.32774
Observations	120	120	120	120	120	120	120

Table 5.1 is expressed overall statistics report of all study variables. The mean of ROA showing sample average of respective variable as overall is 4.135%, this depicted that Rs. 0.04135 earnings will be produced against investment of each rupee one in assets. The other variables like return on equity have higher average upto 9.39% while return on investment average as whole is highest at 15.86% for the sample used.

The maximum value of ROA has 22.75% shows difference of range profitability. While the minimum value of 15.35% displays a loss for some companies. While the maximum value of ROE is 44.97% shows the difference fluctuated from profitability and the minimum value 42.74% demonstrates loss for some companies. The said figures show the difference in profitability among the companies. Hence, the under-review firms describe the outcome and discloses that higher %age in ROE's value than the value of ROA is evidenced that companies are prefer to use more equity than the use of debt. Companies less depend on debt financing. In the table 5.1 ROI at maximum value is 48.95% shows the difference fluctuates from profitability while the minimum value of 21.82% is displaying high loss for some specific companies. The value ROI at 15.86% is evidenced that have low value of %age. While gearing measurement reflects in high mean value of 55.57%. That thing indicates that

companies' liabilities in total on average amount are appraised upto 55.57% the value of total assets.

Matrix of Correlation

In table 5.2 outcomes of the tests applied explained negative correlation among interest coverage as independent variable and ROA (-0.1816), ROE (-0.1518) and ROI (-0.0114) as dependent variables and also ratio of debt (-0.1954) along with ratio of debt-equity (0.2251) upto the level of 0.01 significant correlations exists. While financial gearing at 0.5816 is favorable upto level of 0.05 which reflects theory of agency and show the conflict in between owners and management executives which may cause the low performance. At the significance level of 0.01 ROE as dependent variable has positive correlation (0.0256) with ratio of debt using as independent variable, accordingly at 0.05 levels financial gearing have positive correlation (0.0722) with ROE. This reflects that debt has less risk in the sample having positive effect on owners' equity. On the contrary, at the level of 0.01 of significance the ratio of debt-equity independent variable has negative correlation (0.020). Accordingly at 0.05 level interest coverage also has negative correlation (-0.152) with ROE. This shows that debt amounts are high as compare to equity. It reflects that debt financing has inverse effect on ROE. Hence, lower debt financing makes the high return on equity.

Table-5.2 Overall Correlation Statistics of variables

Correlation Probability	ROI	ROE	ROA	INTEREST _COVER	F_L_ RATIO	DEBT_ RATIO	DEBT_ EQUITY
ROI	1						

ROE	0.879043	1					
	0	----					
ROA	0.812233	0.943479	1				
	0	0	----				
INTEREST _COVER	-0.011361	-0.151805	-0.181594	1			
	0.902	0.0979	0.0471	----			
F_L_RATIO	-0.051092	0.072164	0.058158	-0.058656	1		
	0.5794	0.4335	0.5281	0.5245	----		
DEBT_RATIO	0.273465	0.02558	-0.195427	0.33538	-0.087926	1	
	0.0025	0.7815	0.0324	0.0002	0.3396	----	
DEBT_EQUITY	0.222726	-0.020025	-0.225077	0.306629	-0.115521	0.937516	1
	0.0145	0.8281	0.0135	0.0007	0.209	0	----

On the same way, at the significance level of 0.01 returns on investment using as dependent variable also have positive correlations with ratio of debt and debt-equity by the correlation coefficient of 0.2735 and 0.2227 using as explanatory variables. This reflects that in case if companies' debt increased, it will provide opportunity to permit surety for more borrowings for funds investment in better projects. Conversely, significant correlations are also existed among the explanatory variables. At the level of 0.01 of significance ratio of debt and interest coverage both independent variables have positive correlations (0.335) between each other. Accordingly, ratio of debt-equity explanatory variable is also having positive correlations with other two independent variables ratio of debt and interest coverage by correlation coefficient of .3066 and 0.9375 respectively at same said significance level. These positively correlated variables like debt structure and interest coverage reflects company's capability to permit surety for more borrowings. Hence, companies have much ability to pay the finance cost results in more debt can use.

Hausman Test

For implication of policy and for analytical purpose, another Hausman test is employed to determine the most appropriate model to accept in each under discussion periods. This test analyzes in clarifying having the disparity or not among the three models. In the research study, basically, this test is applied to determine the most appropriate and best model among them for acceptance. The following hypothesis is verified through this test to choose the model to accept.

Hypothesis of Hausman Test:

H0: represents the suitability for Random effect model

H1: represents the suitability for fixed effect model

Notable: Statistically significance value of probability decides to select the fixed effect or Random effect model that which one of the models will be used in the research study.

Table 5.6 Results of the Hausman Test

Correlated Random Effects - Hausman Test Results									
Test Summary	ROA (2011 - 2020)			ROE (2011 - 2020)			ROI (2011 - 2020)		
	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.	Chi-Sq. Statistic	Chi-Sq. d.f.	Prob.
Cross-section random	0.69047	4	0.9525	3.200622	4	0.5248	1.971299	4	0.741
Period random	2.055411	4	0.7256	3.69666	4	0.4486	0.801896	4	0.9382
Cross-section and period random	2.390853	4	0.6643	4.923933	4	0.2952	3.180102	4	0.5282

Source: Using E-Views – 10 software Computation of Author

In table 5.6 while closely observing the values of Chi-Square of above three models where period random, cross section random or both cross-section and period random values are in comparison of dependent variables ROA, ROE and ROI. Firstly, the values of Probability for cross-section random are 0.95, 0.52, and 0.74 respectively which shows that all of these values are greater than 5%. Secondly, the values of Probability for period random are 0.73, 0.44, and 0.94 respectively which shows that one value is below than 5%. Lastly, the values of Probability for both cross-section and period random are 0.66, 0.29, 0.52 respectively here one value is also below 5%. Hence, cross section Random is suitable because in this case null hypothesis cannot reject. The reason is that all the values are higher than 5%. Therefore, Suitable model is Random effect model to accept for analytical purposes.

Random Effects Test Analysis

Table 5.5 Random Effects Models Regression Results Excerpt

Random Effect Model												
Dependent Variable: ROA, ROE, ROI												
	ROA				ROE				ROI			
Variable	Coefficient	Std. Error	t-Statistic	Prob.	Coefficient	Std. Error	t-Statistic	Prob.	Coefficient	Std. Error	t-Statistic	Prob.
DEBT_EQUITY	-0.0249	0.01258	-1.97861	0.050	-0.05418	0.03056	-1.77315	0.079	-0.05488	0.02613	-2.10035	0.038
DEBT_RATIO	0.056639	0.08066	0.702192	0.484	0.300962	0.19316	1.558105	0.122	0.501361	0.1662	3.016602	0.003
F_L_RATIO	3.92E-05	3.55E-05	1.102845	0.272	1.20E-04	8.93E-05	1.346035	0.181	-2.58E-08	7.52E-05	-0.00034	1.000
INTEREST_COVER	0.006174	0.00805	0.766685	0.445	0.000825	0.01995	0.041333	0.967	0.017761	0.01698	1.045943	0.298
C	0.0442	0.0314	1.407509	0.162	0.0072	0.07268	0.099063	0.921	-0.04646	0.06588	-0.70522	0.482

	ROA	ROE	ROI		ROA	ROE	ROI
R-squared	0.085356	0.04484	0.110752	Mean dependent var	0.010	0.028	0.035
Adjusted R-squared	0.053543	0.01161	0.079821	S.D. dependent var	0.034	0.083	0.072
S.E. of regression	0.032605	0.08276	0.069271	Sum squared resid	0.122	0.788	0.552
F-statistic	2.683006	1.3495	3.580681	Durbin-Watson stat	1.970	2.239	1.999
Prob(F-statistic)	0.034948	0.25595	0.008633				

Source: Using E-Views – 10 software Computation of Author

Econometric form of Projected Random Effects Models

ROA = 0.0442 + (-0.0249) X1 + (0.056639) X2 + (3.92E-05) X3 + (0.006174) X4

ROE = 0.0072 + (-0.05418) X1 + (0.300962) X2 + (1.20E-04) X3 + (0.000825) X4

ROI = -0.04646 + (-0.05488) X1 + (0.501361) X2 + (-2.58E-08) X3 + (0.017761) X4

The above table 5.5 is displaying the results of all the three random effect models in order to compare each of them. Evidently, all the explanatory variables, Debt-equity ratio,

debt ratio, F.L. ratio and ratio of Interest cover have significantly favorable influence on firm's performance in all the three models except one variable (debt-equity) which has negative effect on ROA, ROE, and ROI. Therefore, Debt-Equity ratio has negative effect by -0.025, -0.054 and -0.055 respectively on said explanatory variable while Debt ratio, FL ratio (except on ROI significant but negative), and interest cover ratio have positive effect by 0.056, 3.92, 0.006 on ROA, 0.300, 1.20, and 0.0008 on ROE and lastly 0.50, -2.58, and 0.018 on ROI respectively.

All the models regarding overall significance implies the relationship's direction and behavior of dependent variables can be explain with help of explanatory variables which is the integral part for models used in the study. This research study displayed that autocorrelation of Durbin Watson test (1.97, 2.24, and 1.99), regarding the criteria of econometric, is free from autocorrelation's problem in all the three models.

VI. CONCLUSIONS

This study has proven positive relationship among most of the variables. The result depicts that the Textile Sector might increase financial gearing by reviewing its better use of internal and external sources of funds upto upper debt threshold estimate level keeping in view its optimum financial structure. By applying the pooled regression technique, the results illustrate the positive relationship exists between financial gearing and performance (ROA, ROE, ROI) while adverse relationship with ROE. It emphasizes that increasing of external borrowings declines the financial performance which measured with help of Return on Equity. The study outcomes described the adverse relation in concerning nominated firm's financial gearing as well as financial performance. Hence, profit of the firm's decreases when financing in debt increases. Research results explained the adverse relation among ratio of debt, ratio of debt to equity along with ratio of return on assets. Thus, a firm can produce more profits if it reduces external borrowings which are using in the financial structure of the firm.

The researcher extracts and concludes the following on the basis of above said results:

1. By examining the study reveals that a favorable relation exists among the financial gearing with Return on Investment, Return on Equity and Return on Assets. Hence, decisions related to mixture of financing and operating expenses fixed in nature favorably affect the earning capacity and ability of the company to generate revenue. In case when revenues of the company are greater than fixed financial charges payable to investors / creditors, the gearing as a whole positively affect the revenue.
2. Large organizations increase the confidence of the investor in order to add value of the company.
3. Any enhancement in the structure of the assets, keeping in view its importance with the help of strategic decisions, is a positive sign for the stakeholders.
4. The outcomes demonstrate that the ratios related to debt and equity has favorable but irrelevant influence on company's performance in case when it is measured with help of ROA. The ratio related to debt and equity has adverse and substantial relation with performance of the company. Equity returns display favorable and important relation with ratios of debt and equity. Ratio of equity has adverse and irrelevant relation with performance of the company. ROCE or ROI with ratio of debt display adverse and irrelevant relation and debt /equity has favorable and substantial relation.
5. Any Enhancement in financial gearing is caused to reduce the equity value in contrast assets' value rise. The reason is that gearing negatively affect ROE while positively affect ROA. In case where gearing value does not enhance the equity value then gearing has positively affect overall firm's performance.

RECOMMENDATIONS

Based on above said conclusions, the study endorses the following recommendations:

1. The companies related textile sector should associate the concepts of financial gearing and the firm's value along with try to combine both in that manner which is reproduced on earnings.
2. Companies might have to accomplish an optimum mixture of internal and external funds, for endurance in the long run towards the company's growth.
3. While using retained earnings to finance their projects, Companies have to develop fresh strategies in order to enhance the firm's financial performance.
4. External borrowings which are an integral part of gearing should less depend but more concentrate to develop strategies internally in order to enhance the firm's financial performance.
5. The regression outcomes demonstrated the unfavorable relation between financial gearing and financial performance of textile industry. Large organizations produce maximum earnings with respect to organizations small in size. Liquidity and profitability both are positively interrelated. Hence, there may be a vital motive for healthier performance of Pakistani textile companies is the decrease in cost of capital.
6. The authorities of regulatory bodies like SECP and SBP should notice the appropriate level of financial gearing of listed companies of textile as well as banks related sectors towards national level. Keeping in view the international standards the ratio of debt-to-equity should set upto the mark at 40:60. The State Bank of Pakistan may direct the commercial banks to consider said ratio during the issuance of new loans to the textile industrial sector.
7. Some companies face unstable environment during business operations. Because macro-economic variables are uncontrollable, it is highly probable that firms will be operating in an unstable environment. Either way gearing is recommended. In a stable environment, high gearing is recommended. In an unstable environment, lower gearing levels are recommended.

8. By utilizing external sources, with smart planning to finance the company's operations, companies might invest surplus funds in the financial market with help of repurchase agreements to get high returns with respect to cost of investment.

09. Management of the companies should take counteractive action to maximize the margins of profit, assets returns and Equity returns by controlling the levels of debt incase if firm's financial performance diverge extensively lower than the normal pertaining to actual gearing level.

10. Companies have to setup equilibrium in using the equity and debt financing. Profits become low in case of undue use of debt because outstanding payments to creditors increases results in financial performance decreases. While more dividend is paid in case of undue use of equity results in retained earnings reduced which can reinvest in the business to produce more company income towards maximizing the wealth of the shareholders while using the retained earnings can reduced the necessity of financial gearing as high risk is interlink with it.

11. Debt financing is feasible in case it will be used to enhance the present assets utilization. In other words, utilization of assets and debt requirement should be equated and create equilibrium between them by the companies.

12. In the end, to set financial gearing as well as financial structure of the firm along with society standards of calculation is required to investigate in upcoming studies. Hence this research study recommended that a separate study is obligatory to observe the financial gearing and financial structure impact on financial performance as well as society (human resource) for each sector is required, so that more comprehensive knowledge to confirm the relationship among the variables may be available.

SUGGESTIONS FOR FUTURE RESEARCH

Different limited proxies like ROE, ROA and ROI are utilized to observe the organization's financial performance. Forthcoming research scholars may investigate according to financial point of view the gearing, structure and performance relation with help of more comprehensive proxies which are not used during this research in order to compute the variables. The primary data may use irrespective of secondary data in other sectors of Pakistan to investigate gearing, structure and performance relationship as well as to generalize their research outcomes.

Future research scholars may use bigger data of time series as well as techniques of innovative econometric in order to induce implications as well as other different economies like Pakistan, India, Bangladesh etc. to investigate the cross-country analysis as well as in between developed and under developed countries by concentrating more on those businesses which are going through the recession period. Forthcoming researchers can explore causes in the form of gearing and financial structure effect on letting down of Pakistani businesses. In this way imminent researchers may examine the effect of inflation, interest rate as well as tax rates along with GDP on financial performance of the companies. Another way to study future research is to check the firm's financial performance in comparison of Islamic and non-Islamic financing, which can add the knowledge in literature.

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