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www.aarf.asia, **Email** : editoraarf@gmail.com

Review of the Impact of Financing Decisions on Business Performance

Dr Manohar Goel, Associate Professor
Mukand Lal National College
Yamuna Nagar (Haryana)

Abstract: The use of debt or equity to finance the urge of an organization; have always been the matter of debate as these decisions are of irreversible in nature. The present study aims to feed the famine urge of existing literature pertaining to the ambiguous outcomes of measuring the role of funding sources on corporate performance. The study incorporates all the related previous published researches during the tenure of 2008-2020 from the database of Google Scholar, after which certain filtration has been performed. Studies having only selected variables have been elected to make a thorough analysis. The crux of these studies has been served in the format of a tabular literature and concluded that funding choices (DTA) has an adverse influence on fiscal health of the company while the other indicator DER demonstrate a mixed efficacy. Control attributes liquidity, corporate size and growth opportunities have demonstrates an affirmative influence on firm performance whereas tangibility negatively relates with firm performance. The study results can benefits the investors and policy-makers in deciding about the proportion of debt-equity mix.

Keywords: Financing decisions, capital structure decisions, firm performanceand profitability.

Introduction:

Because of how crucial and long-lasting financing decisions are, they have long been a source of intense anxiety. The argument arose after Miller and Modigilani proposed in 1958 that debt-equity decisions are immaterial. In their research, they made some unreal assumptions about perfect markets, which prompted the researchers to do additional research to validate the impacts of using debt on a corporation's value and profitability. However, Modigilani and Miller stated in 1963 that the use of fixed-income securities might result in tax benefits, thereby improving an organization's total yields. However, the outcomes of these investigations create contradicting conclusions in different settings. Since then, numerous theoretical theories and practical research have emerged. Borrowing as a technique of achieving tax benefits has received special attention in trade-off theory (Myers, 1984). However, according to the pecking-order theory, when it comes to addressing the needs of the firm, internal resources are prioritized over external financing options. (Myers and Majluf, 1984). On the other side, agency cost theory as propounded by Jensen and Meckling (1976) favored the use of debt portion in a capital structure to cut down the cost arisen from principle-agent conflicts. They further explained it as the debt-holders can create burden on management to pay back their loans and interest payments timely and ultimately the mangers have to enrich the performance level to meet such expenses which can positively affect the revenue generating capacity of the enterprise.

Various empirical studies have been conducted to examine and verify the actual impact of funding decisions or capital structure decisions on the earning capabilities of the organization. While some studies (Dawar (2014), Nisha and Ghosh (2018), Sutomo et al. (2019)) utilize for greater internal finance, others (Mursalim et al. (2015), Murniati et al. (2019)) advocate for debt or external borrowings. Several studies have found that employing debt or equity has little influence on one's financial well-being. This theory is supported by Modigilani and Miller (1958), Khan et al. (2017), and Domenichelli (2018).

Such conflicting results can be served as a research gap and produce an urge to further elaborate the literature and squeeze the crux out of it. Debt-equity ratio and the debt-assets ratio have been recognized as independent factors whereas liquidity, tangibility, corporate size & growth opportunities have been identified as control attributes of the study. The main implication of research is for investors at the time of making investment choices and for managers to make decisions regarding funding sources choices.

Review of Related Literatures:

To understand the role of financing decisions on the fiscal performance of the organization, it is required to thoroughly examine the previous literatures concerning about the same.

Sr. No.	Authors' Name	Objectives	Research Methodology	Major Findings		
				Positive	Negative	No impact
	Ahmed (2008)	To ascertain the role of financing decisions on performance of 100 composite corporations quoted at Kuala Lumpur stock exchange over the time span from 1999-2002.	Panel Regression Model has been employed to analyze the gathered data. DTA portrays the financing decision while Tobin's Q describes the performance of the corporation.		DTA has an adverse impressio n on Tobin's Q.	
	Amjed (2011)	To explore the efficacy of financial structure choices on performance of 270 chemical sector companies quoted at Karachi Stock Exchange during the tenure of 6 years from 2001 tp 2006.	OLS regression model has been employed for analysis purposes. ROA & ROE has been deployed to gauge the fiscal performance of the concern. STD, LTD and total debt ratios describe the debt-equity mixture of financial structure. Growth opportunities and the size of the organization represented as control variables.	Size and growth rate of the corporation have been positively connected with its performance indicators.	STD & LTD with ROE and ROA portrays an adverse linkage. Total debt also influence the profitabilit y measures negatively .	
	Moradi	To encounter	Simple and	DPR	DTA	

	et. al. (2012)	the influence of corporate governance and choices of funding on profitability efficiency of 84 enterprises quoted at Tehran Stock Exchange over the 5 years from 2007-2011.	multivariate regression analysis has been emphasized. Tobin's Q and ROI indicate the profitability efficiency of the companies whereas funding decisions followed by DPR, DTA, Non-executive member ratio, institutional investor ratio.	affirmatively affect both measures whether ROI or Tobin's Q. Institutional investors with ROI and Non-executives members with Tobin's Q found to have an confirmatory linkage.	adversely affect both profitability proxies (ROI & Tobin's Q). Non-executive members with ROI depict an opposite relationship whereas institutional investors conversely affect Tobin's Q measure.	
	Mursalim et. al. (2015)	To discover the link among funding decisions, innovations, profitability capacity and value of 13 enterprises listed at Stock Exchange of Indonesia during the period from 2008-2013.	Partial Least Square has been adopted. Capital structure, dividend ratio and ROI have been used to demonstrate the financial decisions. MBV and Tobin's Q has been occupied as an indicator of corporate performance and its value.	ROI, Innovation aspect and capital structure ratio indicates an affirmative influence on both Tobin's Q and MBV. Dividend policy also positively affect Tobin's Q.		No considerable influence of dividend policy on MBV.
	Daud et. al. (2016)	To identify the role of financing choice on performance	Balanced Panel data series with multiple regression model. ROA signifies as	Size of the conglomerate demonstrates a	Liquidity connotes a negative effect on performan	DTAportrays a insignificant influence

		of 76 publicaly quoted Malaysian corporations scheduled during the period of 1994-2007.	main proxy for gauging firm performance whereas size, DTA and liquidity as a marker for financing decision.	significant positive reaction on ROA.	ce proxy.	on ROA.
	Ashraf et. al. (2017)	To delve out the efficacy of governance mechanism and funding decisions on profitability proxies of 19 organizations engaged in cement business quoted at Karachi Stock Exchange during the time duration of 11 years from 2006-2016.	Multiple regression technique of econometric models has been employed. NPM, EPS with ROA & ROE recognized as performance proxies whereas DER, DTS, STDR, LTDR, DPR, board size, board meetings, size of firms and managerial ownership has been termed as factors determining the governance and funding decision of a concern.	LTDR, DTR, board size, managerial ownership, DPR with ROA found positively linked. DPR, LTDR, DTR & board size affirmatively affect ROE. Size of firm, DER, DPR, DTR & board meetings with EPS. DER, STDR, LTDR, board size, firm size, DTS upbeats NPM.	DER, STDR, board meeting & size of firm portrays a negative association. STDR, firm size, DER, board meeting & managerial ownership found negatively connected with ROE. Board size, STDR, LTDR & managerial ownership with EPS. DPR, board meetings & manageria	

					l ownership portrays adverse link with NPM.	
	Khan et. al. (2017)	To investigate the influence of financing decisions on performance of Karachi Stock Exchange listed 100 Industrial firms throughout the period of 2004-2009.	OLS regression technique is adopted to accomplish the task. Debt-Equity Ratio signifies the financing decision whereas ROA, Market cap, ROE and Tobin's Q epitomize the performance of the corporation. Size of the concern is taken as control variable.	Size of the organization positively affects the ROE, market cap & ROA. DER affirmativel y linked with Tobin's Q.	Size conversely affect the Tobin's Q.	DER portrays no significan t link with market cap and ROE.
	Domenic helli (2018)	To examine the persuasion of financing choice and corporate governance on performance of 983 large and medium sized family firms operating in Italy.	Multiple regression model has been implemented in which ROA & ROE indicates dependent variables whereas LTD, size, age, STD, debt-equity ratio, solvency as independent ones.	Size positively affects both profitability measures. Solvency positively hits the ROA.	Solvency, debt-equity ratio conveys an adverse relation with ROE. Age negatively affect both parameter s. Debt-equity ratio linked negatively with	LTD & STD describes no link with ROE and ROA.

					ROA.	
	Muiruri and Wepukhulu (2018)	To ascertain the role of funding decisions with investment, liquidity and dividend choices on performance of 66 NSE quoted companies of India during the tenure of 5 years from 2012-2016.	Multiple regression model has been emphasized. DER represents funding decisions, current ratio portrays liquidity decisions whereas DPR signifies the choice of dividend and long term investments represents the investing choices of the concern. While ROA and ROE depicts an association's fiscal performance.	DER positively affects ROE. CR and the choices of investment alternatives, signifies an upbeat relation with both ROA & ROE.		DER insignificant but affirmatively related with ROA. DPR insignificantly but adversely influence both measures; ROA and ROE.
	Murniati et. al. (2019)	To recognize the effect of investing, dividend and financing choices on monetary value of 62 corporations listed under Indonesia Stock Exchange over the tenure of 2012-2016.	SEM has been employed by using financial decisions as exogenous factors whereas profitability and firm value as intervening and endogenous variables respectively.	Financing and investment choices of the firm evidenced as favorable to both profitability & value of the firm.	Dividend choices depicts an insignificant but adverse influence on firm value and its profitability.	
	Sule (2019)	To empirically probe the link of financing	OLS regression technique with leverage as key	Size depicts a positive influence on	Tangibility aspect portrays	Leverage on ROA & ROE

		decisions with monetary health of the organizations working under the FTSE 100 & FTSE 250, of United Kingdom during the tenure of 2015.	independent determinant of financing decision. ROA & ROE as proxy of profitability and tangibility, size as control attributes.	profitability proxies.	an adverse association with profitability.	signifies affirmative insignificant impression.
	Sutomo et. al. (2019)	To identify the determinants of funding sources as well as investigating the link between corporate debt, profitability aspects and growth opportunities of 150 corporations operating at Indonesian Stock Exchange during the time span from 2012-2017.	Path analysis has been employed with the aid of LISREL. ROA as profitability proxy whereas DTA as a measure of funding decision. Risk, growth, investment opportunity and corporate size have been recognized as explanatory variables.	Size, growth rate, investment opportunities and risk factor depicts an affirmative association with profitability.	DTA demonstrate an adverse link with ROA.	
	Afsar and Karacayir (2020)	To explore the influence of financing & investing decisions on profitability of 100	Fixed effect panel regression model has been employed. DTR and current ratio signifies the role of financing	Current ratio found to have a positive efficacy on firm value.	DTR adversely influence the firm value of organizations.	

		companies scheduled under Borsa Istanbul Industrial Index during the tenure of 2003-2018.	decisions while firm value reflected by lastly closed share price.			
	Doan (2020)	To recognize the role of financing decisions on monetary health of 102 non-financial corporations quoted on HOSE (Ho Chi Minh Stock Exchange) for the duration of 10 years from 2008-2018.	GMM model has been executed. ROA signifies the performance measure while LTDA, STDA and TDA represent the financing decisions of the enterprise. Size, rate of inflation & growth of economy used as control factors for the study.	Inflation rate affirmatively affect the ROA.	Short-term, total and long term debt as indicator of financing health, portrays adverse influence on ROA.	Economy growth and company size found to have insignificant effect on ROA.
	Imelda and Himelda (2020)	To examine the efficacy of capital structure while considering financing decisions as mediating factor affecting the monetary wealth of 42 banking organizations operated at Indonesia Stock Exchange over the years from 2016-2018.	T-test with multiple regression analysis has been employed. Tobin’s Q represented as performance indicator while TDR as capital structure ratio. Retention Ratio has been employed as financing decision.	DTR affirmatively connected with Tobin’s Q.	RR negatively associated with Tobin’s Q.	No considerable link has been recognized between DTR and RR.

FINDINGS AND DISCUSSION

To explore the influence of financing or funding decisions on monetary health of organizations, previous literatures have been scrutinized thoroughly and evidenced a sort of mixed outcomes presenting in the form of different variables. Some studies depict a negative association of funding decisions with performance while some signifies an affirmative link among the two. There are studies which shows no or insignificant efficacy of financing choices with firm value. The reason might be the selection of different variables, different sample selection or the prevailing circumstances of different economy.

Based on previous research, it is clear that most studies employ the debt-equity and debt-assets ratios as extra tools to evaluate investment decisions, whereas Tobin's Q, ROA, and ROE are used as major measurements of firm performance. The majority of studies' control variables have been liquidity, growth potential, tangibility, and corporate size. Following a thorough analysis, it was discovered that the debt-to-equity ratio has contradictory associations with a company's profitability variables. The firm of the money raised through debts is dependent on the firm's ability to create profits. Debt will help the firm's financial status if it can generate the income required to repay past-due debts and associated interest. This study's findings are equivalent to those of Ashraf et al. (2017), Khan et. al. (2017) and Muiruri and Wepukhulu (2018), in which they describes that debt-equity ratios signals a mixed (positive and negative) impression on monetary performance of the organization. Another variable debt to assets found to have a negative association with firm performance proxies which means an organisation’s assets are not capable enough to generate sufficient earnings to pay back dues. The findings of the study are in lined with Moradi et. al. (2012), Sutomo et. al. (2019), Ahmed (2008), Amjed (2011), Doan (2020), in which they summarized that debt-to-assets ratio signifies an adverse impression on monetary performance. These studies carry some control variables with them which indirectly influence the financial health of the association. As majority of previous researches indicates liquidity, tangibility of assets, growth opportunities and corporate size as most occurring control variables. As a result, the relationship between these variables and the monetary health of the organization has also been investigated. Asset liquidity improves corporate performance and demonstrates that a company manages its working capital properly. It can help the firm make the most use of its current assets and pay its interest commitments on schedule. The study's findings support those of Muiruri and Wepukhulu (2018) and Afsar and Karacayir (2020), who found that an asset's liquidity has a positive impact on the state of the economy's money supply. However, the conclusions of this study contradict those of Daud et al (2016). The other control variable, asset tangibility, was revealed to have a negative relationship with firm profitability, indicating that the connected firms lack the ability to efficiently manage the ratio of tangible to intangible assets. Sule's (2019) outcomes, which reveal a poor association between debt and monetary performance, are supported by the research. The total value of a company's assets can be estimated to determine its size, which is another significant control variable. The great majority of studies suggest a positive relationship between company size and financial performance.A large sized company found to have a positive impact on its performance. The reason might be the economies of scale enjoyed by the firm at the time of producing large amount of products and a considerable impression on overall market. The s of this research is favored by the findings of Amjed (2011), Daud et. al. (2016), Ashraf et. al. (2017), Khan et. al. (2017), Domenichelli (2018), Sule (2019), Sutomo et. al. (2019). A company’s growth rate is one of its significant aspect and as per the findings of the study, growthopportunities portrays a positive link with fiscal health of a company. The firms having more growth opportunities tends to have a more profitable future as it can invest the funds in most beneficial and favourable opportunity and can multiply the earnings of the company. The result of the study is supported by Amjed (2011) and Sutomo et. al. (2019).

Selected previous literature		DER	DTAR	Liquidity	Tangibility	Size	Growth
Ahmed (2008)	Tobin’s Q		-ve				
Amjed (2011)	ROA		-ve			+ve	+ve
	ROE		-ve			+ve	+ve
Moradi et. al. (2012)	Tobin’s Q		-ve				
	ROI		-ve				
Mursalim et. al. (2015)	Tobin’s Q		+ve				
	MBV		+ve				
Daud et. al. (2016)	ROA		Insign.	-ve		+ve	
Ashraf et. al. (2017)	ROA	+ve				+ve	
	ROE	-ve				-ve	
	EPS	+ve				+ve	
	NPM	+ve				+ve	
Khan et. al. (2017)	ROA	-ve				+ve	
	ROE	Insign.				+ve	
	Tobin’s Q	+ve				-ve	
Domenichelli (2018)	ROA	-ve				+ve	
	ROE	-ve				+ve	
Muiruri and Wepukhulu (2018)	ROA	Insign.		+ve			
	ROE	+ve		+ve			
Sule (2019)	ROA	Insign.			-ve	+ve	
	ROE	Insign.			-ve	+ve	
Sutomo et. al. (2019)	ROA		-ve			+ve	+ve
Afsar and Karacayir (2020)	Closing Price	-ve		+ve			
Doan (2020)	ROA		-ve				Insign.
Imelda and Himelda (2020)	Tobin’s Q		+ve				

Table depicting summarized results of selected studies. (Source: Author’s own Compilation)

CONCLUSION

The present study aims to feed the famine urge of existing literature pertaining to the ambiguous outcomes of measuring the role of funding sources on corporate performance. After a thorough analysis of previous related literatures, mostly occurred determinants representing funding choices and fiscal performance has been identified. To gauge the funding sources of the company debt-equity ratio and debt-assets ratio has been elected whereas to demonstrate the financial health ROA, Tobin's Q & ROE has been chosen. Debt-equity ratio recognized to have a mixed impression on firm performance indicators while debt-assets ratio portrays a negative impression on most of profitability proxies. The control factors of the study embraces liquidity position, tangibility of assets, size of corporation and its growth opportunities. The study deduced that liquid assets make the firm more capable to maintain its reputation by paying debts on time and firm can grab the opportunities accordingly. Also, it is originated that tangibility of assets signifies a negative association with profit earning capacity which indicates that firm's management isn't efficient enough to maintain a balance between tangible and intangible assets. Apart from this, size has also taken as a considerable attribute and deduced that large sized corporation tends to provide a fruitful future due to economies of scale. Same goes with the growth opportunities. Firms have more opportunities for growth can grow better in future as compared to the companies having less opportunity. As per the results of mainstream researches, it can be summarized that funding choices negatively affect the monetary health of an organization.

Every study poses certain limitation with itself, so as this study contains. The outcomes of the study have been driven on the basis of selected past researches which have been elected via hand searched by the researcher. No statistical tools have been applied, as the use of statistical tool can make the results more authentic. Also the time period of the study ranges only from 2008-2020. Further only Google Scholar has been used as a source to collect studies. Future studies can include the whole time span and different databases to make the results more validate.

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