

Debt Financing and Firm Value of Listed Consumer Goods Firms in Nigeria

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Abstract

This study was conducted to ascertain the influence of debt financing on the firm value of listed consumer goods firms in Nigeria. Ex-post facto research design was adopted in the study. The population of this study consisted of twenty-one (21) consumer goods firms listed on the floor of Nigerian Stock Exchange as at 31st December 2019, while the sample size of the study was sixteen (16) listed consumer goods firms in Nigeria. The study covered the financial period of 2013-2019 year of assessment. Purposive sampling technique was adopted in the study. Data were collected from the financial statements of the sample firms in Nigeria. The data collected were analysed using descriptive statistic and multiple linear regression analysis with the help of E-view version 10. Findings from the study showed that Debt Ratio and Long-Term Debt have positive and significant influence on the firm value of listed consumer goods firms in Nigeria. In conclusion, the paper posited that debt financing is a good source of financing for firms in the consumer good industry. However, in view of the opposing implications of debt financing, that is, the cheap option and the risk of default, the paper recommended that listed consumer goods firms in Nigeria should continue to embrace the use of debt in their capital structure as a financial option but with caution so that the investment of equity owners will not be drowned in the ocean of debt servicing and possible bankruptcy menace due to accumulative interest expense and default in repayment of capital

Key words: Debt, Debt financing, Firm, Value and Consumer goods.

Introduction

Investments of hard earned resources have continuously been the option of people in the search for higher economic returns. Some of these investments are given by investors as borrowed funds to select firms in the hope of financial returns in the form of interests. To an investor, financial statements are the main tools used in depicting/showing the financial health and risk of a firm, and these affect investment decisions. One of the outstanding features in a typical financial statement, especially the capital structure section, is debt. Debt is money borrowed from another person or

entity with a view to paying back with interest on an agreed date. Debt is a cheaper source of funding for most companies because it is tax deductible. In view of the fact that companies are allowed to charge interest expense on debt before arriving at the profit for the year, debt financing has become a tempting source of finance to many companies. However, debts have fixed interests and principal commitments which can affect firms negatively if the debt profile grows out of control. In a worst-case scenario, successive default in interest payments could result in financial distress or bankruptcy. In this case, debt holders must be settled first and the equity owners stand the risk of losing their investments. Besides the negative implication of interest default, high debt profile requires surplus cash for debt servicing thereby limiting the ability of a firm to pay dividends. From historical sequence, the heavy use of debt has affected many large firms over time (Pandey, 2013). Therefore, firms must choose the best sources of finance that would enable them to reach the optimal financial structure so that they can make suitable financial decision for positive outcomes.

There are some theories behind debt financing as a financial option. Sajid (2016) observed that the impact of debt financing on the value of the firm has been a puzzling issue. For instance, the tax-based theories introduced by Modigliani & Miller (1958) emphasize on the role of tax advantage of debt financing and argue that the value of the firm would increase with more debt. However, the duo, Modigliani & Miller (1958) are of the opinion that in a perfect capital market, strategies do not affect the value of the firm, hence, they argue that, under very restrictive assumptions of perfect capital markets, investors' homogenous expectations, a tax-free economy, and no transaction costs, the capital structure is irrelevant in determining a firm's value. However, these assumptions look confusing in a real life situation. Some scholars believe that there is an optimal financial structure, but there is no specific method for ensuring that they achieve an optimal debt level, yet financial theory provides some guide for the understanding of how the chosen financing mix affect the firm's value. Arising from this theoretical nexus, firm value can be defined as an economic concept that reflects the value of a business. It is the value that a business is worthy of at a particular date. Theoretically, it is an amount that one needs to pay to buy or take over a business entity (Pandey, 2013). Like an asset, the value of a firm could be determined on the basis of either book value or market value. But generally, it refers to the market value of a company (Pandey, 2013).

Statement of the Problem

Consumer goods industry in Nigeria is expected to be the most stable in the manufacturing sector, but unfortunately, the sector is grappling with series of challenges that have negatively affected the value of this sub-sector. Lack of modern technology, inadequate capital structure, excessive debt financing, lack of electricity, natural disasters and inefficient use of available resources have put consumer goods companies in Nigeria in a very uncompetitive situation.

The delisting of some of the consumer goods firms by Nigerian Securities and Exchange Commission has generated so much worries in the minds of investors, financial analysts and academic researchers and fingers have pointed at the financial institutions and managers on how the affected firms were funded and managed, which led to their being delisted from trading on the floor of Nigeria Stock Exchange (NSE). Consumer goods firms such as Jos International Breweries Plc. in 2016, PS Mandrides Plc. in 2016, Premier Breweries Plc. in 2016 and UTC Nigerian Plc. in 2017 were delisted from the floor of Nigerian Stock Exchange because of their regular failure to meet up with the listing rules and regulations stated in the NSE Rule Book 2015. The affected firms were unable to settle their creditors and the firms' assets were taken over by creditors. The affected firms failed to pay dividend and also failed to file their quarterly and annual financial statements as required by rule 21(1-5) of the Nigerian Stock Exchange Rule Book 2015. According to Onyema (2019), first and second notice were issued to the affected firms for them to improve on their failure but they could not meet the requirement, hence the striking out of their names from NSE list.

Besides the downward trend of the performance in the consumer goods industry, what gave impetus to the present study is that a review of studies conducted on debt financing and firms' value with data from this sector have shown conflicting outcomes. Because of the importance of debt financing as a life wire and financial option for firms, it is needful to conduct this current study with the view to exploring new outcomes in debt capital as a driver of firms' value.

Objectives of the Study

The main objective of this study is to investigate the influence of debt financing on the value of listed consumer goods firms in Nigeria. The specific objectives are to:

- i. examine the effect of debt ratio (DR) on the value of listed consumer goods firms in Nigeria;
- ii. evaluate the influence of long-term debt (LTD) on the value of listed consumer goods firms in Nigeria.

Research Questions

- i. What is the effect of debt ratio (DR) on the value of listed consumer goods firms in Nigeria?
- ii. What is the influence of long-term debt (LTD) on the value of listed consumer goods firms in Nigeria?

Hypotheses of the Study

- i. Debt ratio (DR) has no significant effect on the value of listed consumer goods firms in Nigeria.
- ii. Long-term debt (LTD) has no significant influence on the value of listed consumer goods firms in Nigeria.

Review of Related Literature

Conceptual Review

Debt Financing

In general context, debt financing is the use of debt in a firm's financial structure. It involves the use of fixed-charge sources of funds such as loan and preference share capital along with the owner's equity in the capital structure. Debt financing is also gearing or trading on equity. The use of the term 'trading on equity' is derived from the fact that, it is the owner's equity that is used as a basis to raise debt. Debt financing impose restrictive power on the holders, that is, the suppliers of debt have limited participation in the company's profits, and this make them to insist on protection of the value of their resources by equity owners. In profit sharing, debt holders are first paid, that is their interest are settled before dividend is paid to the equity owners, besides they are also preferred in settlement in case of liquidation. It is therefore expected that owners or equity fund be levered or priced far above the contributions of the debt holders in the capital structure (Pandey, 2013).

Mathematically, if a firm borrows N100 at 8 percent interest rate per annum and invests it to earn 12 percent return per annum, the balance of 4 percent after payment of interest will belong to the shareholders and this constitute the profit from debt financing. On the other hand, if a firm borrows the same amount and invests it to earn 6 percent interest/return on that investment, it means that, the shareholders will lose 2 percent per annum.

Arising from the double implications of using debt capital, it is often said that debt financing is a double edged sword in that it provides the potential for increasing the shareholders' earnings as well as creating the risk for losses in case of default in settlement of timely obligations. In the observation of Abor (2007), debt financing affects not only the performance of the organization, but also the market value of the organizations. Management of debt financing is very crucial in the organization because the funds obtained from creditors have to be returned with interest (Black,

2015). Also, the negative implication of using debt financing is that it could multiply losses when interest payment accumulates. More so, failure to repay debt could result in bankruptcy and complete loss of shareholders' investment. Thus, debt financing must be traded with caution because debt position positively affects return to shareholders in good times and adversely affects them in bad times (Sajid, 2016). This double implication of debt financing makes it needful to assess its impact on firm value of consumer goods in Nigeria.

Types of Debt

There are four main categories of debt. Most debt can be classified as secured debt, unsecured debt, revolving debt and mortgage debt. Secured debt is collateralized debt. Debt givers usually require the collateral to be a property or assets with a large value to cover the amount of the debt (Pandey, 2013). Examples of collateral include vehicles, houses, boats, securities and investments. These items are pledged as security and the agreement is created upon which the collateral may be sold or liquidated with the proceeds used to repay the loan, if the agreement is defaulted. Unsecured Debt is a debt that does not require collateral as security. The credit worthiness and the debtor's ability to repay are reviewed before consideration is given, because there is no collateral assignment that is issued. In this situation, the debtor's credit profile is the primary factor used in determining whether to approve or deny lending. Another type of debt is revolving Debt. Revolving debt is a line of credit or an amount that a borrower can continuously borrow from a given source (Nhung, 2017). In other words, the borrower may use funds up to a certain amount, pay it back, and borrow up to that amount again. The most common form of revolving debt is credit card debt. The card issue initiates the agreement by offering a line of credit to the borrower. In this case, as long as the borrower fulfils his/her obligations, the line of credit is available for as long as the account is active. Mortgage Debt is another debt option. It is a debt issued to purchase real estate such as a house or condo. It is a form of secured debt as the subject 'real estate' is used as collateral against the loan. However, mortgages are so unique that they deserve their own debt classification (Miller, 1977).

Measurement of Debt

Two option in measuring debts are debt ratio and long-term debt. Debt ratio is a financial ratio that indicates the percentage of a firm's assets that are funded by debt. It is the ratio of total debt to total assets. That is: $\text{Debt ratio} = \frac{\text{Total Debts}}{\text{Total Assets}}$

For example, a firm with N3,000,000 in total assets and N600,000 in total liabilities would have a debt ratio of 20%. Total liabilities divided by total assets or the debt/asset ratio, shows the proportion of a firm's assets which are financed through debt. If the ratio is less than 0.5, it means that, most of the firm's assets are financed using equity. But if the ratio is greater than 0.5, it means that most of the firm's assets are financed using debt. Firms with high debt to asset ratios are said to be highly leveraged. The higher the ratio, the greater risk would be associated with the firm's operation. Furthermore, high debt to assets ratio may indicate low borrowing capacity of a firm, which in turn would lower the firm's financial flexibility. Like all financial ratios, a firm's debt ratio should be compared with its industry average or other competing firms (Zhang, 2000).

Long-term debt, on the other hand, is one of the debt ratios that measures the proportion of long-term debt used to finance the assets of a business. This ratio represents the position of debt that the company takes (Bhaumik, 2011). With this ratio, analysts can estimate the capability of the corporation to meet its long-term outstanding loans. Long-term debt ratio also known as long-term debt to total assets ratio is often calculated yearly, as most of the business financial statement comes up once in every fiscal year. This is calculated yearly to determine the company's debt trend. If the ratio tends to rise as the year moves forward, it means that the business is becoming more dependent on debt (Guin, 2011). Another important measure in debt evaluation is long-term debt to equity ratio. This is a leverage ratio comparing the total amount of long-term debt against

the shareholder's equity of a company. The goal of this ratio is to determine how much debt the company is taking. A higher ratio means that the company is taking on more debts. This, in turn, often makes them more prone to financial risks. Long-term debt to equity is variation of the debt to equity ratio. Debt to equity takes into account short-term debt, long-term debt, and other fixed payments. Some analysts prefer the former ratio since long-term debt tend to be more burdening and has more risk compared to other liabilities. In addition, apart from the current ratio, looking at one company's past result is also a good idea. With this, it can be observed whether the level of leverage is increasing or decreasing. Even if a company has a high long-term debt to equity ratio, it can still have a better reputation/value if the ratio lowers year by year (Gujarati, 1995).

Long-term debt can be seen in the liabilities section of the company's financial statement. Long-term debt consists of loans or other debt obligations that are due in more than 12 month or in more than one accounting period. It is necessary to have it at the back of our minds that debt is different from liability. Liabilities include all types of debt, but not all liabilities are debts. Debt is to fund equity, be it an individual or a corporation. It is a borrowed sum that needs to be paid back with an interest when it falls due. Meanwhile, liabilities are something, for instance, money, goods, or service an entity owes to another party that does not required the payment of interest and not always in the form of debt. Other forms of non-debt liabilities are wages and deferred revenue, that is income received by a company when the services are not yet delivered. The shareholders' equity can usually be found on the statement of financial position of a company as well. Shareholders' equity is often called stockholders' equity, owners' equity or simply equity. In terms of corporation, all of these terms refer to the same thing, which is total assets minus total liabilities (Ikechukwu and Nwakaego, 2015). Long-term debt to equity ratio can be vital in determining how risky a business is, for example, it helps the investors and creditors to understand the position of the company in terms of debt, and to decide whether or not to do business with the company (Nissim & Penman, 2001).

Debt Financing and the Shareholders Return

The decision by firms to use debt is often predicated on the possibility of maximizing shareholders' return under favourable economic conditions. The role of debt financing in maximizing the return of the shareholders is based on the assumptions that, the fixed-charges funds such as the loan from financial institutions, banks or debentures, can be obtained at a cost lower than the firm's rate of return on net assets (RRONA or ROI). Thus, when the difference between the earnings generated by assets that is being financed by the fixed-charge funds and costs of these funds is distributed to the shareholders, the earnings per share (EPS) or return on equity (ROE) increases. However, EPS or ROE will fall if the company obtains the fixed-charges funds at a cost higher than the rate of return on the firm's assets. It should, therefore, be clear that EPS, ROE and ROI are the important figures for analysing the effect of debt financing (Shubita & Alsatuahllah, 2012).

Earnings per share (EPS) are calculated by dividing profit after taxes (PAT) or net income (NI) by the number of outstanding shares. PAT is found out in two steps. First, the interest on debt, (INT), is deducted from the earnings before interest and taxes, (EBIT), to obtain the profit before taxes (PBT). Then, taxes are computed and subtracted it from profit before tax (PBT) to arrive at the figure of PAT. The formula for calculating EPS is shown as follows:

$$\text{Earnings per share} = \frac{\text{Profit after tax}}{\text{Number of shares}}$$
$$\text{EPS} = \frac{\text{PAT}}{N} = \frac{(\text{EBIT} - \text{INT})(1 - T)}{N}$$

Where T is the corporate tax rate and N is the number of ordinary shares outstanding. If the firm does not employ any debt, then the formula is shown as follows:

$$\text{EPS} = \frac{\text{EBIT}(1 - T)}{N}$$

ROE is obtained by dividing PAT by equity (E). Thus, the formula for calculating ROE is shown as follows:

$$\text{ROE} = \frac{\text{Profit after tax}}{\text{Value of equity}}$$
$$\text{ROE} = \frac{(\text{EBIT} - \text{INT})(1 - T)}{E}$$

When calculating ROE, it is either the book value or the market value of equity may be used.

The use of debt capital is important to corporate value. A number of companies in practice prefer to borrow for several reasons such as tax deductibility of interest, higher return to shareholders due to gearing, complicated procedure of raising equity capital, none dilution of ownership and control, less commitment than equity capital. There are, however, managers whose choice of finance depends on internal and external factors. The internal factors include: purpose of financing, company's earning capacity, existing capital structure, cash flow ability and investment plans etc. while the external factors are: capital and money market conditions, debt-equity stipulations followed by financiers and restriction imposed. A company for instance may feel that, there is no specific preference towards borrowings as a source of finance. The company's financial requirement would vary from time to time depending on factors such as its existing capital structure, investment plans, expansion, modernization and replacement as also its margin money requirement for incremental working capital. In addition, the cost of share issued, existing money market, banking conditions and the impact of statutory regulations would influence the mix of finance required by a company. In practice, it may not be possible for a company to borrow whenever it wants. Lenders may analyse a number of characteristics of the borrowers, before they decided to lend. Borrowing firms perceive the following factors in order of importance being considered by the lenders: profitability, quality of management, security, liquidity, existing debt-equity ratio, sales growth, net worth, fluctuation in profits and reserve position (Stulz, 2014).

Many firms engage in debt financing because of the benefits involved. Some advantages a firm might enjoy in using debt to finance its assets are cost reduction resulting from the fact that interest on debt is tax deductible, fixed return which exclude debt holders from sharing more profits during seasons of high performance, restriction of debt holders from voting right, maximising financial returns. However, the use of high debt ratio leads to greater risk (financial risk) and higher interest rate is required to compensate for the additional risk. Also debt financing increases shareholders' risk as it concentrates the firm's business risk on the shareholders, because debt-holders who receive fixed interest payments bear none of the business risk. However, debt financing will enhance shareholders' returns on the condition that the fixed charges funds such as the loan and debentures can be obtained at a cost lower than the firm's rate of return on net assets (Margaritis & Pislaki, 2008).

Firms' Value and Firm Value Determination

Maximizing shareholders' wealth is one of the corporate goals that cannot be ignored. The market value of a firm is an important measure of the shareholders' wealth. Firm's valuation is essential for deriving stock prices and item of significance in many models. The value of a firm is basically the sum of claims of its creditors and shareholders. Therefore, one of the simplest ways to measure the value of a firm is by adding the market value of its debt, equity, and minority interest while cash and cash equivalents would be deducted to arrive at the net value.

With respect to firm value determination. Kanwal & Nadeema (2013) maintain that stock price, sometimes, is the sole measure of performance in the model. More commonly, it is a major component of a weighted average that includes other measure. The value of a firm can be obtained through different measures, each of which is likely to give a value that differs from that obtained by another. The first and most readily available measure of the value of a firm is its accounting net worth or book value. This measure is however problematic because the accounting rule in a model

may be at variance (in divergence) with generally accepted principles of financial accounting. This is because conformance with some generally accepted principles such as historical cost and conservatism, can lead to values that are far from what is reasonable. The second measure is the market value of all its outstanding shares. This is popular in everyday world method of valuating public corporations. Its application however requires an efficient real market for shares. This condition is not met in models that do not allow participants to trade shares, and even when such trading is allowed, the trades are generally too few and too infrequent for reliable valuation. The third measure is the capitalized value of its projected future performance (Masa'deh et al. 2015).

Modigliani & Miller (1958) pointed out that, although four distinct methods of capitalization can be applied for this purpose and all of them give rise to precisely the same valuation when the markets are perfect. People are completely rational, and the future is known with perfect certainty. However, the capitalized valued measure has a problem as it requires at least one arbitrary parameter (m), if the Goosen's method is applied. The fourth measure is the deductive application of human judgment. With this method, firms are rated along a psychometric scale. The results are then converted by formula to monetary values. The problem of this measure is that, it requires subjective judgment. The fifth measure is the firm's accounting net worth adjusted for intangible and the idiosyncrasies of accounting rules used in the simulation. Although, general principle could be laid out for the adjustment, the specific principle must depend upon the particulars of the model.

Though, the adjusted net worth measure avoids both problems. It does not require arbitrary parameter and can be completely objective. Its problem however, is that it requires detailed knowledge of imitation used in any particular model. However, the market value measure of determining firms' value is the most reliable and straightforward way of determining a firm's value. It is also known as market capitalization. that is, total value of all shares outstanding. It should be noted that this method only works for publicly traded companies, where shares value can be easily determined. The market capitalization (market value) of a firm can be determined by multiplying the number of outstanding shares by the current stock price. For example, let us consider Multi-Trex Integrated Food Plc whose share price is 0.36k and the outstanding shares is 3,722,493,620. Therefore, Multi-Trex market capitalization is 0.36k multiplied by 3,722,493,620 equal to 1,340,097,703. The above illustration shows that the major rider of a firm's value using this measure is the stock price.

Long-term Debt and Firms' Value

Ross et al. (2004) stated that the value of a firm is the value of its assets plus the value of tax benefits enjoyed as a result of debt, minus the value of bankruptcy cost associated with debt. Modigliani (1958) pointed out that, the value of the firm is the sum of its debt and equity and this depends only on the income stream generated by its assets. The value of the firm's equity is the discounted value of its shareholder's earnings called net income. That is, the net income divided by the equity capitalization rate or expected rate of return on equity. The net income is obtained by subtracting interest on debt from net operating income. On the other hand, the value of debt is the discounted value of interest on debt (Zaidi et al. 2019). Zhang (2000) suggested that, when firms have more internally generated funds than positive net present value (NPV) projects, debt forces the managers to pay out funds that might otherwise have been invested in negative net present value projects. This over-investment problem can be lessened if managers are forced to pay out excess funds for servicing debt, therefore enhancing the firms' value.

Myers & Read (2012) suggested that a firm with outstanding debt may have the incentive to reject projects that have positive NPV if the benefits from accepting the project accrue to the bondholders without also increasing shareholder's wealth. Gill & Mathur (2011) stated that seeds of under-investment problem lie in the solution of over-investment of U.S firms. They discovered that for

firms with high profitability to equity (P/E) ratios or for high-growth firms, value is negatively related to leverage and those firms with low profitability to equity (P/E) ratios or for low-growth firms, value is positively related to leverage. Their evidence supports the contention that for low-growth firms, leverage acts as a monitoring mechanism to enhance firm value. Whereas for high-growth firms' leverage causes under investment and destroys the value of the firm. The above empirical studies show that there is a relationship between debt and firms' value.

Theoretical Review

This section provides an overview of the theories adopted in the study. Three theories were adopted in the study. The theories are: Agency Theory (AT) 1976, Trade Off Theory (TOT) 1984, and Tobin's Q Theory (TQT) 1969.

Agency Theory

One of the defining characteristics of a business in the 1990s was the adoption of the agency cost theory to address the managerial excesses of the 1970s and 1980s. The classical agency concept was propounded by Jensen & Meckling (1976). They observed that ownership and control which have been separated in larger corporations as a result of dilution in equity positions provided an opportunity for professional managers to act in their best interest. Thus, the agency cost theory attempted to provide explanation to firm behaviours in the area of choice financing. Despite the earlier works of Berle & Means' research in 1932, their analyses permitted the building up of interlink between the organization and the agency theory of corporate finance. Since the vast literatures on the agency theory's explanations of financial structure have been developed, much of the activities of management are associated with increasing the size of the organizations and management were motivated not by a desire for maximizing shareholder's wealth but by opportunities for the self-aggrandizement, therefore, contractual device was suggested by agency cost theory to the shareholders.

Thus, debt provides a means of bonding managers promises to pay out future cash flows as well as providing the means for controlling opportunistic behaviour by reducing the cash flows available for discretionary spending, ensuring that top managers' attention is then clearly focused on those activities necessary to ensure that debt payments are made. A performing firm is one that borrows and is capable of honouring its commitment without any serious problem; by contrast, a bad firm is one that acts.

Agency cost theory also has important implication for the relationship between equity holders and debt holders. Thus, while equity holders are interested in the return over and above the amount which is required to repay debt, debt holders are only interested in debt payment specified in the contract. Also, it is seen that most equity holders are sometimes interested in pursuing riskier business activities that debt holders would prefer. When this occurs, debt holders may charge higher prices for the capital and this constitutes greater control measures to prevent top managers from investing in capital in riskier undertakings.

Some scholars such as Stulz (2014) have provided further development to the agency cost model. In his work on hypothesis, he stated that the firm is in possession of important cash flows generating abundant liquidity, thus supporting the idea of an optimal financial structure of financing that would result from a compromise between benefits related to the reduction of cash flows and the inconveniences that this cash flows relate to the reduction of cash flows and the nuisance that this cash flows may be so weak when investment opportunities are good.

The estimated conflicts between shareholders and managers can result from disagreements in optimal resources allocation. Thus, firms with stronger liquidity value with less cost of information are more likely to contract new debts. This would lead them to rapidly experience failure thus favouring their control by investors. A new approach to test the agency cost theory was studied by

Allen & Wharton (2002). According to them, agency costs represent important problems in corporate governance for both financial and non-financial industries, they assumed that the agency theory suggest that the choice of financing structure may help mitigate these agency cost. To them, under the agency cost hypothesis, high debt or a low equity asset ratio reduces the agency cost of outside equity and increases firms' value by constraining or encouraging managers to act more in the interest of shareholders. They were of the view that greater debt financing may affect managers and thus reduce agency costs through the threat of liquidation which causes personal losses to managers, loss salaries, low reputations, pressure to generate cash flows to pay interest expenses etc.

Elliot (2002), in supporting the agency cost theory states that shareholders of a company are the true owners and that the duty of top management should solely be, to ensure that shareholders interest is met. In other words, the duty of top managers should be to manage the company in such a way that returns to shareholders are maximized thereby increasing the profit figures and cash flows. In trying to outline problems that exist between management and shareholders, managers use the excess free cash flows available to fulfil their own personal interest instead of increasing returns to the shareholders. As a result of that, this theory is very useful in this study.

Trade off Theory

Trade off theory (TOT) was developed by Myers & Majluf (1984). This theory reveals an idea of a company on how to choose how much debt finance and how much equity finance to be used in balancing costs and benefits. The root of this theory goes back to Kraus & Litzenberger (1973) when they considered a state preference model of optimal debt financing and a balance between the dead-weight costs of bankruptcy and the tax saving benefits of debt. This theory is often set up as a competitor theory to the pecking order theory of capital structure. The essential aspect of this theory is to explain the fact that firms usually financed partly with debt and partly with equity. The marginal benefit of further increases in debt declines as debt increases, while the marginal cost increases, so a firm that optimizing its overall value would focus on this trade-off when choosing how much debt and equity to use for financing.

The empirical relevance of this trade-off theory has often been questioned. Miller (1977) compared this balancing as akin to the balance between horse and rabbit content in a stew of one horse and one rabbit. Taxes are large and they are sure, while bankruptcy is rare end, according to Miller, it has low-weight costs. Furthermore, he suggests that if the trade-off theory were true, then firms ought to have much higher debt levels than we observe in reality. Myers was particularly a fierce critic in his presidential address to the American Finance Association meetings in which he proposed what he called the pecking order theory.

Fama & French (2002) criticized both the trade-off theory and the pecking order theory in different ways. Welch (2004) argued that firms do not undo the impact of stock price shocks as they should under the basic trade-off theory hence the mechanical change in asset prices that make up for most of the variation in capital structure. Despite such criticisms, the trade-off theory remains the dominant theory of corporate capital structure as taught in the main corporate finance textbooks. The dynamic versions of this theory generally seem to offer enough flexibility in matching the data, contrary to Miller's verbal argument and it is very hard to reject empirically. Therefore, this theory has a very good relevance in this study as it provides an overview of the matching concepts between cost of debt and its benefits to the management of listed consumer goods firms in Nigeria where this study was carried out.

Tobin's Q Theory

This theory was postulated by James Tobin in 1969 and he used it as a measurement of performance. This theory specifies the percentage of the firm's financial performance as a ratio of

the market value to the replacement cost of the firm's value. Tobin's used this model to measure the performance of the company since it contains a combination of accounting book value and market value of information and seems to be free from managerial manipulation. This proxy was derived from the product of the firm's share price and the number of common stock shares outstanding plus the firm's preference stock plus total net debt divided by the book value of the total assets of the firm. Under Tobin's Q theory, a firm is said to create market value if the company's return on investment is greater than the cost of investment.

Therefore, Tobin's Q (TQ) is a reflection of the market anticipation about future profitability against return on assets or gross profit margin basis, which is connected to current profitability. The theory further explained that a low value of Tobin's Q that is between 0 and 1 could suggest that the cost to replace the firm assets is greater than the value of its stock. Mathematically, it could mean that the share is undervalued. On the other hand, a higher Tobin's Q that is greater than 1 implies that firm's share is more expensive than the replacement cost of its assets, which also could suggest that the share is overvalued. Therefore, in this current study, the paper adapted Tobin's Q as a proxy for firm value since it has all what it takes to give an authentic value of listed consumer goods firms in Nigeria.

Empirical Review

In this section, the focus is on the evaluation of some of the research works done by other researchers in this area of study.

Aamir et al. (2021) conducted a study on debt financing and firm performance of Pakistan Stock Exchange. The purpose of their study was to investigate the relationship between the listed firms' debt level and performance from the period of 2013 – 2017. The researchers used pooled ordinary least square regression and fixed random effects models to analyse a cross-sectional sample of thirty (30) Pakistani companies operating on the Pakistan Stock Exchange (PSX). The result of their study indicated that, both short term and long term debt had negative and significant impacts on firm performance. This suggested that agency issues may lead to a high-debt policy, resulting in lower performance. However, both sales growth and firm size have positive effects on the profitability of non-financial sector companies. The researchers concluded that, company owners and managers should find a satisfactory debt level when debt financing significantly and negatively influences firm performance. They recommended that, the external source of financing should be the last option for management.

Akaji et al. (2021) examined the effect of debt financing on performance of firms in Nigeria. The researchers measured debt financing using the variables of long-term debt financing (LTDF), short-term debt financing (STDF) and preferred stock financing (PSF). Three hypotheses were formulated to guide the study. The design used in the study was *ex-post facto* research design while data for the study were collected from the annual reports and NSE fact book. The collected data were analysed using ordinary least square (OLS) statistic. Findings showed that, debt financing has significant and positive effect on firm's performance in Nigeria at 5% level of significant. The researchers concluded that, debt financing has improved firm's performance over the years. Based on this, it was recommended that, firms should try to finance their investment activities with debts and consider equity as a last option. They further stated that, firms should be debt intensive in their financing decisions as it influences performance.

Anshu & Narendra (2015) conducted a study on financial leverage and firm value of listed manufacturing sector firms in Mahila, India. The objective of the study was to examine the impact of capital structure on the selected Manufacturing sector firms and its effect on the value of the firm. The researchers stated that, capital structure decision is crucial for understanding the dynamics of business growth for any business organization because organizations are oriented towards maximizing output as it has greater impact on a firm's ability to deal with its competitive

environment. This study synthesized the capital structure determinants theory and empirically examined both determinants and suggested firm behaviour patterns in relation to financing decisions of 145 Manufacturing Sector Firms for the period of 2001-2009. The analysis was carried out using a relatively new and innovative factor-analytic structural equation modelling (SEM) methodology. Findings revealed that non-debt tax shield is considered as an important determinant of financial leverage and it was verified that Manufacturing Sector Firms with high non-debt tax shield use more debt as compared to other Manufacturing Sector Firms. The return on capital employed was highest in MSFCS Sector among all Manufacturing Sector Firms resulting into higher profitability, maximizing the shareholders' return and impacting the firm value. The research concluded that the Manufacturing Sector Firms Capital Structure is too rigid to offer any scope for adjustment.

Aniefor & Onatuyeh (2019) examined the effect of debt financing on the corporate performance of listed consumer goods firms in Nigeria. The researchers stated that, the concept of debt financing has assumed considerable importance in recent years given the fundamental role debts play in forming the financial structure of corporate firms. Data for the study were collected from the audited annual reports of fifteen (15) consumer goods firms listed in the Nigerian Stock Exchange (NSE) for the period of 2006-2017. The data were analysed using descriptive statistics and panel regression technique. Findings showed that, total debt, long-term debt and short-term debt to asset ratio positively influenced the performance of consumer goods firms in Nigeria. The researchers recommended that, there is need for the Nigerian firms to rely less on short-term debts, which forms the major part of their leverage, and focus more on developing internal strategies that can help improved their performance.

Gayan (2016) investigated the impact of financial leverage on firms' value. The main objective was to compare the value of the firms of the listed manufacturing companies in Sri Lanka by using the financial leverages for estimations. Data were collected from secondary source. A sample of ten listed manufacturing companies was considered with 50 observations for the period of 2011-2015. Financial ratios were calculated and Pearson's correlation, descriptive analysis of variance and regression analysis were utilized in testing the hypotheses and to measure the differences and similarities between the manufacturing companies according to their different characteristics. The results indicated that, there is a significant relationship between DE ratio and ROA. According to Pearson correlation, there is a weak negative relationship between DE ratio and ROA. Also that there was no significant relationship between DE ratio and ROA. The researcher recommended that, empirical studies should be undertaken in the same field to find out how financial leverages could affect firms' value of manufacturing companies in Sri Lanka.

Josephat et al. (2011) conducted a study on the impact of debt financing and value of firms in developing countries. Their study was on the present and potential investors that needed information for their investment decisions, which included the value creating potentials of relevant firms. They stated that, the information produced was to help investors to estimate the value of the firm which in turn would aid the process of investment decision making. It was from this background that their study examined the impact of debt financing on the value of Nigerian firms adopting a bankruptcy model as a measurement for dependent variable. The study was based on the historical accounting data obtained from the financial statements and accounts of 28 quoted firms on the Nigerian Stock Exchange and covered the period of 2004-2008. A bankruptcy model and multiple discriminant analysis (MDA) were adopted and the benchmark of 2.675 Z score was used to enhance the value or not. The result from their findings revealed that, twenty firms had value created as a result of external funds in their financial mix; eight firms did not create value under the same condition. Therefore, the use of debt financing enhances the value of selected firms in Nigeria. They study recommended that, firms should be encouraged to make an effective financing decision in order to magnify the contribution to their economic growth and development.

Lenny & Tsholofelo (2020) investigated the impact of debt financing on financial performance of retail firms listed on Johannesburg Stock Exchange for a period of 2010–2019. The researchers stated that extant literature showed contradicting results on the financing structure for retail firms. Longitudinal research design was adopted while data were collected from secondary source which is the annual reports/financial statements of the selected firms in South Africa. Convenience sampling technique was adopted to select seventeen retail firms listed on the Johannesburg Stock Exchange (JSE) based on the availability of data within their study period.

The independent variables in their study include: lagged return on equity, long term debt to total asset, total debt to total assets, growth in sales and firm size. The method of data analysis was descriptive and inferential statistic and findings showed that size and long term debt to total asset had a negative influence on the financial performance of retail firms, which is consistent with the trade-off theory, and inconsistent with the pecking order theory. According to them, the possible reason could be that, most established retail firms prefer internal source of financing such as equity over debt. Findings further showed that lagged return on equity, total debt to total asset and growth in sales influence the financial performance of retail firms listed on the Johannesburg Stock Exchange (JSE) positively. The study recommended that, retail firm managers should be careful when considering options for financing and should preferably use internal source of financing rather than the external source of finance.

Magoro & Abeywardhana (2017) conducted a study on debt capital and financial performance of listed companies operating in the wholesale and retail sector of South Africa. The researchers used panel data sample of twenty- five (25) South African wholesale and retail sector companies to examine the effect of debt capital on the financial performance of listed companies over the period of 2011 – 2015. Fixed – effects (within) regression model was adopted to measure profitability and financial performance. Finding from the study confirmed that debt capital in terms of short-term debt and long term debt had a negative effect on the financial performance of wholesale and retail sector companies of South Africa.

Ming & Zuwe (2011) applied the Generalized Method of Moment (GMM) to examine the effect of leverage on firm values and contextual variables influencing on this relationship. They make use of 645 companies listed in Taiwan Securities Exchange (TSE) from 2000-2009. The researchers used panel data to estimate the estimator, while the hypotheses were tested using pooled regression technique. The empirical results showed that, the values of leveraged firms are greater than that of an unleveraged firm, if bankruptcy probability is not considered. Secondly, if the benefit and cost of debt is not considered simultaneously, then the leverage is significantly and positively related to the firm's value before reaching firm's optimal capital structure. Thirdly, the positive influence of leverage to the firm's value tends to be stronger when the firm's financial quality is better, that is greater than Z-score. The researchers concluded finding could provide insight into the firm debt finance decision to maximize the firm value. They further added that, if firms decided to finance their asset through debt capital, the future growth and opportunity must take into consideration all the contextual variables which influence the effect of leverage on the firm's value.

Nhung (2017) examined the impact of financial leverage on firm performance using oil and gas companies in England as a case study. The main objective of the study was to investigate the effects of debt ratios on the firm performance through employing a data of 99 financial statements of 18 British Oil and Gas companies from 2009-2014. The two dependent variables used in this research work were: return on assets (ROA) and return on equity (ROE), while the three independent variables used were short-term debt to total asset (STD), long term debt to total asset (LTD), total debt to total asset (TD). Besides, the author also used one control variable which is growth and its proxy by the total assets. The researcher used multiple linear regression analysis in

the study. The result revealed that, there was a strong negative impacts of financial leverage measured by LTD and TD on the performance of ROA and ROE, while STD had insignificant effects on ROA and ROE of these firms. The research concluded that, based on the results of the study, the firms that has a higher level of long term debt and total debt tend to show poorer performance of return on assets and return on equity. The researcher recommended that, in order to obtain a wealthy performance, these firms should be careful in deciding on optimal capital structure where both elements of bankruptcy cost and cost of capital can be minimized.

Nurul-syuhada *et al.* (2019) examined the influence of debt financing on firms' performance using consumers' product industry in Malaysia. The purpose of their study was to investigate the influence of debt financing on firms' performance in the consumer product industry in Malaysia. The firms' performance was measured based on return on assets (ROA), while the independent variables examined were accounts payable (AP), short-term debt (STD), long-term debt (LTD), and firm size. The data for this research were collected from consumer product firms in Malaysia that are listed by Bank Negara Malaysia. Fifteen years of data, from 2001-2015, were analysed. Simple random sampling technique was adopted by the researchers and the data collected were analysed using descriptive statistic and regression analysis. Findings revealed a significant relationship between short term debt and long-term debt on the performance of consumers' product firms in Malaysia. However, an insignificant relationship was found between account payable and firm's size on the performance of consumer product firms in Malaysia. The researchers stated that, other factors can be considered when measuring the performance of consumers' product firms in Malaysia. It was concluded in the study by the researchers that, the result of their research work can be useful to consumers' product firms in Malaysia to make a better financing decision. They recommended that, next research should improve by adding other variables that can influence firm's performance of consumers' product.

Ogbulu & Emeni (2012) conducted a study on the impact of capital structure and firm's value. 124 companies quoted on the Nigerian Stock Exchange (NSE) as at 31st December, 2007 were used as a sample size. Ordinary least squares method of regression was employed in this analysis. The result of the study revealed that, in an emerging economy like Nigeria, equity capital as a component of capital structure is irrelevant to the value of a firm, while long-term-debt was found to be the major determinant of a firm's value. From the findings of this study, corporate financial decision makers were advised to employ more of long-term-debt than equity capital in financing their operations since its results in a positive firm's value.

Shamsuddeen *et al.* (2019) examined the effect of debt financing on firms' value of listed companies in Nigeria using panel data analysis for the period of 2008-2017. The researchers used correlational research design in their study. The population of the study consisted of 300 firms. The researchers sourced data from annual accounts and reports for the study. Enterprise value and earnings before interest and tax debt to asset ratio (EV /EBITDAR) were used as a proxy for firm value. The result from their study showed an insignificant effect on the short-term debt to total assets ratio on firms' value while the ratio for long-term debt to total assets, total debt to total assets and total debt to total equity showed positive effect on firms' value. The board size and firm growth showed no significant effect on firms' value whereas, firm size showed a negative effect on firms' value. From the findings of their study, the researchers concluded that, capital structure influence the firms' value of listed firms in Nigeria. The researchers recommended that, to reduce information asymmetry and moral hazard, managers of firms need to be mindful of the significance of transparency measures, which can improve their affairs with financial institutions in the business environment.

Methodology

This study was carried out using *ex-post facto* research design, while the population of the study consisted of all the none-durable consumer goods firms listed on the floor of Nigerian Stock Exchange as at 31st December 2019. They are twenty-one (21) none durable consumer goods firms

in Nigeria. Sample size of this study consisted sixteen (16) consumer goods firms listed on the floor of Nigerian Stock Exchange (NSE). This is because, out of the total population of twenty-one (21) consumer goods firms listed in Nigerian Stock Exchange as at 31st December 2019 only sixteen (16) of them had up-to date financial statements that was needed in this study. Purposive sampling technique was adopted to select the sample size of sixteen (16) consumer goods firms based on the availability of financial statements. The sixteen consumer goods firms chosen were those with the most active indices and complete financial data for the period of the study. Data for this study were sourced from the annual reports/financial statements of the sampled firms used in the study. Panel data was used and it covered the period of 2013-2019 financial year of assessment.

Measurement of Variables

The measurement an *apriori* expectation of independent and dependent variable of debt financing and firm value of listed consumer goods firms in Nigeria are shown below:

Table 3.1: Measurement of Vari ables

S/N	Variables	Types	Abbreviation	Measurement	<i>Apriori</i> Expectation
	Firm value	Dependent	FV	Tobin's Q= $\frac{MVE+BVD}{\text{Total Assets}}$	
1.	Debt Ratio	Independent	DR	$\frac{\text{Total Debt}}{\text{Total Assets}}$	+
2.	Long-term Debt	Independent	LTD	$\frac{\text{Long-term Debt}}{\text{Total Assets}}$	+

Source: Researchers Compilation (2022).

Empirical Specification of Model

Dependent Variable

The dependent variable in this study is firm value and is proxied by Tobin's Q.

$$TQ_{it} = \frac{MVE + BVD}{BVTA}$$

Where:

- TQ_{it} = Tobin's Q value of firm i in year t
- MVE_{it} = Market value of Equity i
- BVD_{it} = Book value of Debt i in year t
- BVTA_{it} = Book value of total asset i in year t.

In order to conduct an investigation that has to do with the ascertainment of the relevance of debt financing and firm's value, the model is stated as follows:

$$FV = \beta_0 + \beta_1 DR + \beta_2 LTD + e_t \tag{equation (3.1)}$$

Where:

- FV = Firm Value (dependent variable)
- DR = Debt Ratio (independent variable)
- LTD = Long-term Debt (independent variable)
- β₀ = Constant Term (intercept)
- β_{it} = Coefficient of the explanatory Variables
- e_t = Error term (stochastic term)

Method of Data Analysis

The data obtained were analysed using descriptive statistics, multiple linear regression model, correlation coefficient (r), R-Square, Adjusted R-Square, t-statistic (t-stat), Variance Inflation Factor (VIF), Tolerance, Durbin-Watson (DW) statistic, F-ratio and P-value. These methods of data analysis were suitable in this study because it allowed the researcher to establish the influence of debt financing on the value of listed consumer goods firms in Nigeria. Hence, the analysis was carried out at 5% level of significance and decision rules are: Accept H_0 and reject H_1 when P-value is > 0.05 , accept H_1 and reject H_0 when P-value < 0.05 .

Data Analysis

The various statistical tools were used to determine empirical evidence from the presented data.

Descriptive Statistics

For the purpose of describing the nature of the sourced data, the descriptive statistics for each of the variables were computed and presented in Table 4.1:

Table 4.1: Descriptive Statistics

Statistics	FV	DR	LTD
Mean	56.610	0.5656	0.1253
Median	7.0990	0.5635	0.1135
Maximum	877.41	1.5040	0.5040
Minimum	-3.2000	0.1820	0.0000
Std. Dev.	177.56	0.1942	0.0910
Skewness	3.7974	0.8068	0.9787
Kurtosis	15.977	6.5341	4.4375
Jarque-Bera	1055.03	70.436	27.524
Probability	0.0000	0.0000	0.0000
Sum	6340.4	63.347	14.033
Sum Sq. Dev.	3499357.0	4.1849	0.9193
Observations	112	112	112

Source: Researchers Computation (2022)

Table 4.1 Showed descriptive statistics result of dependent and independent variables in the study.

Regression Analysis and Test of Hypotheses

For the purpose of testing the individual linear models of the study as well as the hypotheses, the regression analyses were conducted and the outputs were presented in individual Tables.

Test of Hypothesis One

The regression analysis was conducted to test the model and the results were presented in Table 4.2.

Table 4.2: Linear Regression Output

Variable	Coefficient	Std. Error	t-Statistic	Prob.
DR	144.9602	54.01055	2.683924	0.0050
C	25.37883	51.45442	0.493229	0.6228
R-squared	0.433656	Mean dependent var		56.61039
Adjusted R-squared	0.424531	S.D. dependent var		177.5549
S.E. of regression	176.1047	Akaike info criterion		13.19773
Sum squared resid	3411417.	Schwarz criterion		13.24628
Log likelihood	23.01729	Hannan-Quinn criter.		13.21743
F-statistic	10.835600	Durbin-Watson stat		0.340826
Prob(F-statistic)	0.005032			

Source: Researchers Computation (2022)

Table 4.2, showed that Debt Ratio (DR) had a positive and significant influence on Firms Value (FV) of listed consumer goods firms in Nigeria. This was because the t-statistic and p-value indicated that, DR was significant on FV, where the positive implication was derived from the coefficient of DR (beta-value) in the model. The direction of DR on FV was in compliance with the *a priori* expectation stated by the researcher. The constant value of 2537.88% showed the level of FV as DR was zero and was insignificant.

The null hypothesis, which stated that, debt ratio (DR) does not significantly influence firm value (FV) of the listed consumer goods firms in Nigeria, was rejected and the alternative hypothesis, which states that debt ratio (DR) significantly influence firm value (FV) of the listed consumer goods firms in Nigeria, was accepted on the basis of t-statistic and p-value computed.

Test of Hypothesis Two

The regression analysis was conducted to test the model and the results were presented in Table 4.3.

Table 4.3: Linear Regression Output

Variable	Coefficient	Std. Error	t-Statistic	Prob.
LTD	287.7431	80.73725	3.563945	0.0007
C	20.55772	28.44772	0.722649	0.4714
R-squared	0.419238	Mean dependent var		56.61039
Adjusted R-squared	0.402452	S.D. dependent var		177.5549
S.E. of regression	176.4096	Akaike info criterion		13.20119
Sum squared resid	3423239.	Schwarz criterion		13.24973
Log likelihood	22.12666	Hannan-Quinn criter.		13.22089
F-statistic	12.44592	Durbin-Watson stat		0.316853
Prob(F-statistic)	0.000703			

Source: Researchers Computation (2022)

From Table 4.3, Long-Term Debt (LTD) had a positive and significant influence on Firm Value (FV) of listed consumer goods firms in Nigeria. This is because of the fact that, the t-statistic and p-value indicated that LTD had a significant influence on FV, where the positive implication was derived from the coefficient of LTD (beta-value) in the model. The direction of LTD on FV was in compliance with the *a priori* expectation stated by the researchers. The constant value of 2055.77% showed the level of FV as LTD was zero and was insignificant.

The null hypothesis, which stated that long-term debt (LTD) does not significantly influence firm value (FV) of the listed consumer goods firms in Nigeria, was rejected and the alternative hypothesis, which states that long-term debt (LTD) significantly influence firm value (FV) of the listed consumer goods firms in Nigeria, was accepted on the basis of t-statistic and p-value computed.

Discussion of Findings

From the analysis conducted in this research, Debt Ratio (DR) showed a positive and significant influence on the firm value (FV) of listed consumer goods firms in Nigeria, since the t- statistic is greater than 1.966 and the probability value is less than 0.05 (t-stat.> 1.966 and P – value < 0.05). This means that, a percentage increase in Debt Ratio (DR) brought about 14496.02% increase in firm value (FV) of listed consumer goods firms in Nigeria. This finding is in line with the findings of Aniefor & Onatuyeh (2019) that long-term debt and short-term debt to asset ratio were positively influence the performance of consumer goods firms in Nigeria, despite the fact that their study was on corporate performance while the present study is on the entire firm value of listed consumer goods firms in Nigeria.

It has been further observed from the analysis that, Long-Term Debt (LTD) had a positive and significant influence on Firm Value (FV) of listed consumer goods firms in Nigeria. This is owing to the fact that the result of t-statistic computed is greater than 1.966 and the probability value is less than 0.05 (t- stat. > 1.966 and P-value < 0.05). This also indicates that, a percentage increase in Long-Term Debt (LTD) brought about 28774.31% increase on firms' value of listed consumer goods firms in Nigeria. This finding is in line with the findings of Shamsudden et al. (2019) of a positive and significant influence on the firm value of listed companies in Nigeria. This finding is also in line with the finding of Xicang *et al.* (2012), where long-term debt was found to be the major determinant of firm's value.

Business Implication of Findings

The major business implication of findings from the analysis is that the positive nexus between debt financing and firm value help to sustain the growing concern need of business which will insulate the firms from being delisted from Nigerian Stock Exchange (NSE). Furthermore, findings of this study might clear some doubts in the minds of investors and creditors that debt is the possible cause of failure, consequently, an encouragement to continue to do business with the firms.

Conclusion

From the analysis and findings obtained from this study, debt ratio and long-term debt have positive and significant influence on firm value of listed consumer goods firms in Nigeria. Debt financing is a good source of financing a business. It is pertinent for the firms to source for loan capital as a possible financing option. From the outcome of this study, it could be inferred that debt financing is not the possible cause of failure of some consumer goods industries resulting in the delisting of some of these firms from Nigerian Stock Exchange. It is posited that their failure might be associated with managerial issues which further studies could further explore.

Recommendations

Based on the analysis and the research findings of this study, the researchers recommended that:

- i. Listed consumer goods firms in Nigeria should continue to embrace the use of debt as financing option because it accrues positive and significant impact on firms' value.
- ii. In view of the benefits of debt financing on the scourge of interest expense of debt, government should prevail on creditors, especially, financial institutions to reduce their lending rate as this will contribute to better performance of listed consumer goods firms in Nigeria as well as accrue positive economic growth in the country at large.

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