

The mediation effects of capital structure: Evidence from Malaysian and Indonesian economic sectors

ABSTRACT

We study the comprehensive, simultaneous interrelationships between countries, economic sectors (i.e., primary, secondary, and tertiary sector), capital structure and firm financial performance, especially involving the mediation effects in different sectors. We find that some determinants of capital structure do not only directly enhance firm financial performance. Firm financial performance is also influenced by how capital structure from the product category in the economic sectors have been financed. We find a significant relationship between capital structure and firm financial performance in the secondary and tertiary sectors but not for the primary sector. We find that the secondary sector tends to use internal financing while the tertiary sector tends to use external financing to enhance firm financial performance. Our results also reveal that the effect of capital structure on firm financial performance tends to be mediated by firm- and countryspecific attributes, as well as by the sector in which they operate. A closer examination of the data showed that in the economic sectors, we find robust results that there are not just positive direct and indirect effects, but also negative direct and indirect effects. It should be well understood by financial managers that secondary and tertiary sectors plays an important role in the mediation effect. The contribution of this study is to help the firm manager to make a good decision on the proportions of their capital structure.