Pecking order theoretic determinants of debt levels: evidence from Taiwan

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Abstract

The pecking order theory of capital structure is one of the most influential theories of corporate finance. The purpose of this study is to examine the relationship between pecking order factors and the debt level of Taiwan’s electronic firms. Generalized least squares model is used to estimate the regression model. This study examines the determinants of debt decisions for 137 Taiwan electronic companies that are quoted on the Taiwan Stock Exchange for the 4-year period of 2004-2007. The results indicate that the determinants of total leverage are profitability, growth, tax and size. The negative relation of profitability and debt level implies that firms probably prefer to use these earnings to finance their activities and thus use less debt capital. In the short-term financing decisions, the important determinants are tax, assets structure, and profitability. There is negative relation between margin tax rate and debt level. It indicates that the use of debt has tax shield but also increase the firm’s bankruptcy risk. The important determinants of long-term leverage are assets structure, tax and profitability. The relation between assets structure and debt level is positive. The assets structure ratio shows the ability of the firm to deal with its long-term debt. This consists with the pecking order theory.

Keywords: Corporate finances, Capital structure, Pecking order, Taiwan