Chapter 5: Conclusion and Recommendations

5.1   Summary and Conclusion

The study of debt maturity structure is a relatively new field in the capital structure research. Most of the studies focus mainly on developed markets. This study examines the validity of these studies, using a sample of 260 firms with 1300 observations from 2005 to 2009 in an emerging market, Malaysia. The main theories of debt maturity such as agency cost, the matching principle, signalling, liquidity risk and tax effects are examined. The results generally confirm the agency cost and signalling and liquidity theories as major determinants of the debt maturity structure of Malaysian firms. The results show that the size of the firm, asset maturity and leverage all have positive and significant impact on debt maturity while the effects of firm quality and liquidity risk are negative and significant.

Based on the results large firms and firms with more tangible assets have a higher debt ratio. Larger firms tend to issue public debt which has a longer maturity than private debt. The reason could be the lower issuing cost of public debt which is fixed and independent of the amount of debt. On the other hand small firms rely more heavily on bank debt that typically has shorter maturity than public debt. Firms tend to match the maturity of their debt to the maturity of their assets and signal their quality by using more short-term debt.

Liquidity plays an important role on debt maturity decisions of Malaysian firms because of the need to avoid costly and lengthy bankruptcy process. The results of the leverage confirm the managerial objective of reducing bankruptcy risk because the high leveraged firms tend to borrow on long-term basis. The positive and significant relation between leverage and debt maturity support this notion.

The growth opportunity has the predicted effect on debt maturity although the results are statistically insignificant which would suggest that the underinvestment problem is mitigated by bank monitoring and lowering leverage instead of reducing debt maturity (Myers, 1977). Banks are known to be more efficient than public debt markets in terms of monitoring because their close relationships with their borrowers would allow them to assess precisely the riskiness and quality of firms. The study does not support the proposition that effective tax rate has an impact on debt maturity which might be an outcome of underdeveloped and illiquid debt market or the control of state over industrial firms and banks.

The result of the explanatory power of independent variables show that standard firm specific variables account for large portion of changes in debt maturity ($R^2 =$ 77.85%) but debt maturity structure of Malaysian corporations may also depend on other factors such as corporate ownership structure, macroeconomic factors, market related factors, the financial environment, regulations, and corporate governance traditions of the country.

5.2   Limitations of the Study

This study has some important limitations. First, variations in debt maturity are examined across all of the firm's outstanding debt while more powerful tests might be done by examining the debt maturity variation at issuance. Second, the definition of the amount of debt that matures in more than one year is taken to analyze the maturity choice and this definition tends to treat long-term debt as homogeneous while many debt issues have provisions including the options to modify the repayment schedule that make them essentially heterogeneous. For example debt covenants such as affirmative covenants allow the lender to accelerate the payment schedule if the borrower breaches the covenant. Therefore, such a measurement problem would introduce a potential bias if the use of these provisions is correlated with independent variables. Third, some firms consider the recurrent component of short-term debt as long-term debt in their balance sheet and some of them use creative accounting to reduce their reported debt. So, there are some accounting difficulties in measuring long and short-term debts. Finally, the size of the sample used is small compared to the whole listed companies in Bursa Malaysia.

5.3   Suggestions for Future Research

Although the results of this study are consistent with the findings of other empirical researches, some questions remain unanswered to advance further research. Future researches must focus on the influence of equity market condition on debt maturity structure because managers consider equity market conditions when deciding debt maturity. Equity market condition might be represented by share price performance and equity risk premium (the cost of equity in relation to the return on a risk-free investment. The debt maturity of the Malaysian firms must be compared to other countries with emerging markets because there are cross-country differences in variables which imply the variations in the practices of corporate financial differences in different countries.

Another fact that must be considered in future researches is testing whether corporate managers in Malaysia consider market conditions before deciding the maturity of loans. For doing this test the effects of market equity premium, stock market return index, term structure of interest rate and the volatility of interest rates on loan maturity must be considered. Corporate ownership and control variables also can be added to the future analysis. More consideration is incorporating other aspects of corporate financial policy such as the debt priority structure, the debt-equity decisions of firms and the choice between private and public debt.

5.4   Implications

This study could be useful to the business managers especially in Malaysian firms by identifying the firm-specific determinants of debt maturity structure and their relationship with debt maturity. Knowing the relationship between firm characteristics and debt maturity structure helps managers in making vital decisions to achieve their respective optimal debt maturity structure. Consequently, firms could enjoy the benefits of a better control in agency cost and signal appropriate information about its quality. As a starting point, the recommended model could provide a mean in establishing the optimal debt maturity structure for firms.