



Capital Structure And Financial Performance Of Selected Consumer Good Firms In Nigeria

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Abstract

Decision on gearing is a very important aspect of Corporate Financing process which cannot be overemphasized by any organisation because of its implications on the performance and long run organisational survival. This study analysed the connection between Nigerian manufacturing companies' financial structure and performance using design of ex post facto research. Secondary sources of data for Eight (8) Nigerian manufacturing companies that are listed and have been operating for at least 8 years considering their performances as reflected in their shares for ten years (2015 to 2024) sourced from their published financial statements. Response variable was ROA, a proxy for financial performance calculated as Profit/Total Assets, while independent variable was Capital structure proxy Equity Ratio and Debt Ratio. Analysis including descriptive statistics and correlation matrix were carried out. The outcome of the analysis using Pooled Ordinary Least Square showed that both equity ratio and debt ration positively and significantly impacted return on assets of the selected manufacturing companies under review, the study recommended that Firms should seek professional advice from time to time to fix capital structure that will always maximise shareholders wealth, minimise cost of capital and increase firm's value.

Keywords: *Capital Structure, Financial Performance, Equity Ratio, Debt Ratio, Return on Asset*

1. Introduction

The composition of shareholders fund and debenture is a very crucial decision that can help a firm to achieve its goals (Barakzai, 2025). Although the level of debt and equity maintained by companies varies over time. Wise firms however try to keep their financing mix close to a targeted capital structure (Brigham & Chrdarl, 2016)

Ahmad et al. (2022) viewed capital structure as the blend of the proportion of sources of financing which an enterprise can access. One of the major determinants of cost of capital is capital structure and the measure of risk a corporation is been exposed to is premised on cost of capital (Salwa,2025). The decision on the choice of the composition of the two sources vis-à-vis debenture and owners' equity to an extent dictates firm's value as well as the wealth of the shareholders (Ajayi & Obisesan, 2020). Poor capital structure according to the authors, may lead to decrease in the economic benefits derived by a firm from strategic assets. The decision on capital structure, which is an important aspect of fundamental financing decision affects both financial performance as well as the returns accrued to the providers of funds (Adeoye & Olojede, 2022).

The way the capital is structured according to Modigliani and Miller (1964) Capital structure preposition, is less important to the performance of the firm. The theory is based on the assumption of perfect market, however, imperfect market and behavior in real life situation rendered the theory invalid and this provided a room for the emergency of trade theory of optimal capital structure. Pecking Order introduced asymmetry information and hierarchy financing sources there by replacing trade off model. The goal of all these theories was to find out the linkage between the way the capital of a corporation is composed and how it performs financially. Unfortunately, there is still conflicting submissions on how both are related. Firms should decide optimal capital structure mix which maximises their objectives (Abdulkarim & Bahamman, 2022).

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Capital structure is defined by Brigham and Houston (2016) as the ratio of each type of investors supplied capital with the total equal one. The interaction of how capital is structured and performance in term of finance has been an issue of serious concern among the researchers across the globe. Performance in terms of finance can be attained base on the manner the capital of a company is structured. The role of consumer goods companies that are quoted in the development of any economy is very crucial. They create job opportunities, add to foreign earnings, government revenue and at large contribute to Gross Domestic Products (GDP). The performance and the stability of this sector therefore needs not to be trivialised. Capital structure is considered as one of the determinants of their stability and long run survival. The capital structure decision issue is not limited to only consumer good firm but extend all establishments. The most important aspect of this decision is therefore the determination of suitable composition of shareholders' funds and long-term loan financing, that will maximise the financial performance of the firm.

Several researchers have examined the way capital is structured interacts with the performance in terms of finance both in Nigeria and outside Nigeria, using various sectors as case study, different methodologies, yet the outcome remain inconsistent and inconclusive. Some studies ascertained positive relationship (Babalola et al.; Vy & Nguyet, 2017, Nwannunu, 2022: Oke & Fadaka, 2021), while others established negative relationship (Barakzai, 2025: Prenaj et al. 2024: Shobha & Subhash, 2023: Asen et al., 2021) Main-while Kemble et al. (2025) concluded that Capital structure implication on of Corporation financial performance vary according to the industry. The divergent opinions of previous studies on the nature of the relationship between these two variables creates literature gap, which the research attempts to fill. To achieve this, the study employs most recent data covering relatively longer period duration and larger number of firms than the ones employed by most of the previous studies carried out on Nigeria and other countries to the best knowledge of the researcher as recommended in the study carried out by Babalola et al. (2022) to further investigate whether capital structure impacts financial performance of listed consumer goods in Nigeria.

Empirical and Theoretical Review

Three subheadings are discussed in this section as follows:

Conceptual Review

Capital Structure and Financial Performance

Financing decision is one of the critical decision areas in any organisation, and the manager must pay serious attention to this decision area. Financing decision is majorly concerned with the choice of the most suitable financing mixture for the organisation (Ajayi & Obisesan, 2021: Barakzal, 2025)

A firm Capital Structure is typically defined by Brigham and Houston (2016) as the percentage of each type of investors-supplied capital with the total equal 100%. Brigham and Chrhardt (2016) viewed it as the mixture of debt and equity. According to Adeoye and Olojede (2023), the proportion of shareholders fund and long-term loan employed to finance the formation of an organisational assets is known as capital structure. Meanwhile Hassan and Abubakar (2022) simply put it as the combination of finance sources which a company can access to finance business activities and capital investment.

Giving the important of this crucial aspect of financing decision, deciding on the appropriate mixture of equity and debt capital that will form the capital mix of a firm in order to achieve organisational objectives is a critical aspect of managerial and financing decision (Arikewuyo et al., 2019).

Capital Structure components are basically Equity and Debt. Equity is the fund provided by the shareholders; it reduces risk improves cash flows. Debt on the other hand is long term loan borrowed by a business from external source. Debt has advantages of low cost since interest on it is deductible and the interest is fixed, if the company turns out to be more successful, the profit of the firm is not subjected to sharing. However, there is a risk of company been taking over. Firms with volatile earnings and operating cash flows limit debt usage while Firms with stable cashflows and low business risk will enjoy taking more debt.

The solution is therefore capital mix of both sources, which is the capital structure and the manager task is determination of optimal capital structure. Ahmed et al., (2023) stressed that optimal capital structure limits financial resources cost, improve overall returns and increase shares value. Business risk, tax rates among others are few factors that determine capital structure. Capital structure decision is a continuous one which is required when a firm needs fund to finance investment or project. Although, there is no particular standard capital structure, it varies, because some business with Emmert and clear revenue streams and real estate business required more of debt.

The most important thing is therefore to design the capital mix to maximize the market value of the Corporation involved. A good capital structure according to Vy and Nguyet (2017) is the structure that constitutes a good combination of both debenture and shareholders fund with the intention of maintaining lowest WACC. Financial Performance is the degree of financial objectives being achieved, which is a crucial part of financial risk management. Capital mix decision affects cost of capital, the risk and profitability, maximize net economic returns as well as the value of the share. Expenses incurred for the payment of debt is between the operational expenses and net profit, hence a firm with large proportion of debt without clear streams of revenue will pay high interest and this will reduce net profit (performance)

A robust and well-structured capital mix minimizes overall cost of finance, increases shareholders wealth while an excessive debt to equity ratio leads to financial distress with negative implication on the performance metrics. Therefore, there is a need for robust policy on the capital mix resolution in the overall interest of the establishment.

Theoretical Review

Pecking Order Theory

The proposition was made by Gordon Donaldson in 1961 but was improved by Stewart C. Myers and Nicolas Majluf in 1984. as optional to trade off theory, which affirmed that inverse correlation subsists between firm's financing choice and its performance. The theory is premised on assumption that managers are more informed about their firms than the owners of the business due to disparity of the information (asymmetric information), debt could hence be embraced only when the managers are certain about their organisation's future prospects but consider equity when such prospect is in doubt

Salwa (2025) stressed that the model suggested hierarchy in the choice of financing, choosing sources with least cost and risk. The hierarchy order is internal fund, short term loan, before long term debt. The company's managers prefer internal source and manage their dividend pay out ratio to meet up with the available investment opportunities.

Therefore, when a company is profitable with reasonable earnings, it can consider lower debt in the mixture of its capital structure. because there is an advantage of financing investment from its retained earnings. There is therefore possibility of inverse relationship between debt level ad performance in terms of finance.

Findings from previous empirical studies have demonstrated that pecking order model explained appropriately the correlation between capital mix and firm's Performance financially though, the model is not without its own limitation of laying more emphasis on the order in which the firms access sources of financing and ignores other factors such as tax shield benefits as well as restriction on debt. Hence the choice of the model for the study.

Empirical Review

Numerous studies have been carried out to probe into how capital structure impacts financial performance in different countries and different sectors:

Barakzai (2025) looked in to how financial performance is being influenced by choice made on capital structure in Turkish food, textile and fabricated metal firms for ten years (2011-2020). Independent variable, capital structure was represented by current liability as well as long-term loan while regressand proxy asset's returns (ROA) as well ROE. The outcome of the study demonstrated that there was negative interaction between debenture and the performance of the sector under study. This outcome is consistent with previous studies and agreed with agency cost theory and disregarded Pecking order theory that the manner a firm performs financially is not determined by its capital mix.

Salwa (2025) enquired into how Corporation financial performance is been affected by the way capital composed in Egypt for duration of five years (2019-2023) for forty listed companies in Egyptians Stock Exchange Financial performance proxy Tobi Q, ROA, and ROE whereas capital mix proxy short term debt (STD) ratio and debt to equity ratio. Fixed effects regression model was used to carry out the analysis on the collected secondary date. The results showed that STD and LTD negatively and significantly impacted ROA, while Debt Equity Ratio significantly and negatively impacted ROE and STD on Tobi Q. The outcome of the study affirmed Pecking order theory. However, capital structure may have inverse relationship with the financial performance as proposed by the theory but indirectly the manner the capital of an organisation is structured may improve the financial performance.

Prenaj et al., (2024) looked in to capital mix impact on the performance of Corporations financially in Kosovo. Regression methods pooled OLS Fixed effect and Random effect were adopted o analysis the secondary information sourced via the Financial Statement published results indicated that the choice capital is composed has a weak implication on the financial performance of selected establishments in Kosovo. The result is agreed with the submission of pecking order theory,

Ahmed et al., (2023) enquired into the interaction between capital mix as well as industry's financial performance in Tehra. Secondary information gotten through public yearly reports of selected listed production firms on Tehran Stock exchange for 2011- were processed using a fixed effected regression model. The study's results affirmed that the way capital is composed is inversely connected to financial performance in the chosen firms also affirming pecking order theory preposition.

Asiedu (2021) investigated capital structure impact on 36 listed companies in Nigeria for twelve years adopting two step system GMM and Fixed effect model, The study's outcome demonstrated that of the study revealed that profitability and liquidity ratios are inversely related with debt ratio among the selected non-financial industry selected for the research. Firm size as well as tangible assets of the firms however positively impacted the ratio of debt in the considered organizations. The outcome affirmed mixture of agency cost and pecking order theories.

Okeke and Fadaka (2021) examined the way the capital composition influenced the financial performance of the consumer product firms in Nigeria. The data sourced from the secondary data for 18 listed consumer goods Corporations in the Nigeria Stock Exchange were evaluated using panel data method. The outcome indicated that firm financial performance has inverse interaction with capital structure, growth and performance had a positive correlation for the companies selected in Nigeria, supporting agency cost theory and negating pecking order theory.

Ajayi and Obisesan (2020) examined the way the capital is structured affected financial success of Nigerian companies. Twelve companies were considered for 5 years duration. Some macroeconomics variables impacts were considered. Transaction capital structure theory was embraced to evaluate the significant of leverage and macroeconomic variables on firms' financial performance. A Static panel analysis with the aid of Fixed Effect Regression estimation model. The result demonstrated an important and inverse correlation between leverage and financial performance for the period and the firms under study thereby affirming pecking order preposition.

It is observed from the empirical review that most of the empirical studies uphold the preposition of the pecking order theory which shifts attention from optimal capital structure to cost of asymmetry, resulting in predictable financing hierarchies which indirectly influences performance. Prioritising internal funds, and then debt follow by equity will lead to suboptimal structure, lower leverage in profitable firms and cash hoarding and creating economic effects like potential underinvestment, missed tax shields and agency issues.

Several studies have been carried out internationally and in Nigeria on financial performance of organizations using different sectors with little coverage on consumer goods sector. In addition, the data period horizon the population size employed by most previous studies are shorter to the best knowledge of the researcher. This study therefore filled this gap by employing most recent data, longer data horizon and more firms than most of the previous studies.

Materials and methods

The research uses both descriptive and inferential statistics to examine how Nigerian manufacturing businesses' capital structure and performance are related. Eight (8) listed Nigerian manufacturing companies that have been in operation for at least ten (10) years were selected based on their performance as reflected in their shares. Secondary data for ten years (2015 to 2024) for these firms were sourced from their published financial statements. The experimental variable is financial performance represented by ROA calculated as Profit/Total Assets, while independent variable is capital structure proxy Equity Ratio and Debt Ratio.

In terms of model estimate, the connection between the capital composition and financial performance in consumer goods corporations was examined using static panel regression analysis. More precisely, the static panel estimation approaches for common effect (CE), fixed effect (FE) and random effect (RE) estimator were used. Depending on the fixed effect test, random effect test using Breusch and Pagan Lagrangian multiplier (BP-LM) test and Hausman test results, one can choose which of the previously mentioned approaches to use. Afterwards Post estimation tests involving cross-sectional dependence (CD) test (using Friedman test), heteroscedasticity tests (using Breusch-Pagan/Cook-Weisberg and modified Wald test) and autocorrelation test (Jochmans portmanteau test).

Model Specification

The specific functional models for the study are formulated as stated below:

$$ROA_{it} = f(ER_{it}, DR_{it}, SIZE_{it}) \quad (3.1)$$

Where

- ROA = return on assets (Profit / Total Asset)
- ER = Equity ratio (Equity/ Asset)
- DR = Debt ratio (Debt/ Asset)
- $SIZE$ = firm size

$t = 2015, \dots, 2024$ (annual time series)

Subscript $i = 1, 2, \dots, 8$ (separate production Corporations)

Consequently, the following is the expression for the panel data regression models:

$$ROA_{it} = \beta_0 + \beta_1 ER_{it} + \beta_2 DR_{it} + \beta_3 SIZE_{it} + \mu_{it} \quad (3.2)$$

β_0 , = intercept coefficient

β_j ($j = 1, 2, 3$) = Partial slope coefficient of ROA with respect to ER , DR and $SIZE$.

The selection of the model is based on the fact that it aligns with the research objectives and questions and it is capable of achieving validity, reliability and replicability of the findings. In addition, it is grounded in existing literature and theoretical frame work.

Results

Descriptive Statistics

The descriptive statistics is given in this segment (summary statistics) of the study's variables, including ROA , ER , DR and $SIZE$.

Table 1: Descriptive Statistics
Sample: $N = 8, T = 10$ (2015 - 2024)

| Statistics | Variables | | | |
|-------------|-----------|---------|---------|--------|
| | ROA | ER | DR | SIZE |
| Obs. | 80 | 80 | 80 | 80 |
| Mean | 0.226 | 0.200 | 0.082 | 19.021 |
| Maximum | 4.928 | 0.649 | 0.652 | 23.753 |
| Minimum | -3.547 | 0.000 | 0.000 | 15.935 |
| Std. Dev. | 1.527 | 0.223 | 0.115 | 1.600 |
| Skewness | 0.6455 | 0.7248 | 2.3691 | 0.6306 |
| Kurtosis | 4.1948 | 1.9891 | 10.6278 | 3.3283 |
| Jarque-Bera | 10.3148 | 10.4109 | 268.782 | 5.6612 |
| p -value | 0.0058 | 0.0055 | 0.0000 | 0.0589 |

Source: Computation of Researcher (2025)

Table 1 reports the variables of the panel's summary statistics, revealing that except for Firm Size ($SIZE$), the standard deviations of ROA , Equity Ratio (ER), and Debt Ratio (DR) exceed their respective means, indicating high variability across the selected manufacturing firms. The distributions of all panel variables are positively skewed. Furthermore, with the exception of ER , the variables exhibit platykurtic distributions, characterized by kurtosis coefficients below 3. The Jarque-Bera test for normality suggests that, except for $SIZE$, the panel variables do not conform to a normal distribution, as evidenced by insignificant test results (p -values > 0.05), thereby violating the normality assumption.

4.2 Test of Multicollinearity

Multicollinearity of the explanatory variables was also checked using the Variance Inflation Factor (VIF). VIF indicates the extent to which the estimate of variance of an explanatory variable is inflated by co-relations with other explanatory variables, which is an indicator of whether the multicollinearity exists.

Table 2:- Variance Inflation Factor
Sample: $N = 15, T = 12$ (2015 - 2024)

| Dependent Variables: ROA | | |
|----------------------------|-----|-------|
| Variable | VIF | 1/VIF |

| | | |
|-----------------|--------------|-------|
| DAR | 1.702 | 0.588 |
| EAR | 1.644 | 0.608 |
| SIZE | 1.046 | 0.956 |
| Mean VIF | 1.464 | . |

Source: Researcher’s computation (2025).

The VIFs and tolerance (1/VIF) between the regressor is presented in Table 2. Since it is a general rule, any variance inflation factor below the bearable range of 10 shows the existence of low of multicollinearity (strong relationship) among the variables. It emerges that all VIFs are within standard requirement in regard to the low dependence of the explanatory variables (capital structure). The above implies that the individual and discrete performance will be influenced by the measures of the capital structure.

4.3 Model Estimation

Following the study’s empirical structure, this study employed the static panel data estimators such as common effect (CE) estimator, random effect (RE) and fixed effect (FE) using least square dummy variable (LSDV) estimator variant, with panel structure of 8 consumer goods firms ($N = 8$) for a period of 10 years ($T = 10$) ranging inclusively between 2015 and 2024. Table 4.3 displays the summary of the estimates and statistics acquired from the study’s model estimation using the above-mentioned estimators. The model involves the nexus between performance (ROA) and capital structure. Following the fixed effect test result (F -stat. = 27.300, $p = 0.000 < 0.05$) between the CE and FE estimators, FE estimator appears to be more appropriate as compared with the CE estimator. Similarly, the random effect test (BP-LM stat. = 113.33, $p = 0.000 < 0.05$) between the CE and RE estimators, the RE estimator was found to be more efficient than the CE estimator. Meanwhile, the Hausman test result ($\chi^2 = 1.840$, $p = 0.6070 > 0.05$) indicates that the RE effect estimator appears to be more suitable as compared to the FE estimator. Overall, given the three tests, the **random effect estimator (RE)** appears to be the most efficient estimator among the three (3) contending static panel estimators, and thus, adopted in conducting the study’s inferential analysis. The selection of the RE estimator suggests the presence of heterogeneity among the consumer goods firms.

Table 3-: Panel Model Estimation Results
Panel Structure: $N = 8$, $T = 10$ (2015 - 2025)

| Estimator: | CE | FE: LSDV | RE |
|---|----------------------|----------------------|----------------------|
| Dependent Variable | ROA | ROA | ROA |
| Independent Variable | | | |
| <i>Intercept</i> | -14.87*** (0.000) | -16.58*** (0.000) | -16.49*** (0.000) |
| <i>ER</i> | -0.518*** (0.009) | -0.300** (0.0164) | -0.318*** (0.008) |
| <i>DR</i> | 0.370* (0.062) | 0.375*** (0.001) | 0.373*** (0.000) |
| <i>SIZE</i> | 0.795*** (0.000) | 0.914*** (0.000) | 0.905*** (0.000) |
| Further Statistics and Tests | | | |
| Effect Tests | | | |
| CE-FE: Fixed Effect test (F-Stat.) | - | 27.300*** (0.000) | - |
| CE-RE: BP-LM Test (X^2) | - | - | 113.33*** (0.000) |
| RE-FE: Hausman Test (X^2) | - | - | 1.840 (0.6070) |
| Explanatory Power | | | |
| R-squared | 0.6768 | 0.8817 | 0.8815 |

| | | | |
|--|----------------------|----------------------|-----------------------|
| Adj. R-squared | 0.6614 | - | - |
| F-statistic (or Wald Test) | 43.980*** (0.000) | 139.11*** (0.000) | 422.29*** (0.0000) |
| Diagnostics | | | |
| CD Test: Friedman test | - | 6.627 (0.469) | 6.818 (0.448) |
| Heteroscedasticity test | 0.170 (0.6809) | 6.920 (0.1127) | - |
| Autocorrelation Test (Jochmans Portmanteau) | - | 8.000 (0.998) | 8.000 (0.998) |

Source: Researcher's computation (2024)

Note: The values in the parentheses () are *p*-values of the respective coefficients and statistics while ***&** denote statistical significance at the conventional 1% and 5% levels of significance, respectively.

Test of Individual Significance

As shown in Table 3, the ROA model estimation under the RE estimator demonstrates that equity ratio (*ER*) has a statistically strong significant and negative impact on ROA ($\beta_1 = -0.3178, p = 0.008 < 0.01$) suggesting higher equity financing is associated with lower return on assets, possibly due to the higher costs associated with equity issuance. Specifically, a 1% increase (decrease) in *ER* leads to about 0.32% decline (rise) in ROA, indicating that *ROA* is negatively inelastic with respect to *ER*. The foregoing empirical outcome is consistent with the Pecking Order Theory, which posits that firms prioritize internal financing and debt over equity. However, model estimation shows that debt ratio (*DR*) exerted a statistically significant and positive impact on ROA ($\beta_2 = 0.3732, p = 0.000 < 0.01$) implying that leverage enhances firm performance via ROA, likely due to the tax benefits and discipline imposed by debt servicing. More specifically, a 1% increase (decrease) in *DR* yielded about 2.81% rise (decline) in *ROA*, thus, indicating that *ROA* is positively inelastic with respect to *DR*. The foregoing result supports the Pecking Order Theory's prediction that firms prefer debt financing over equity financing when internal funds are insufficient. Meanwhile, changes in firm size (*SIZE*) yielded a statistically significant and positive impact on *ROA* ($\beta_3 = 0.9054, p = 0.000 < 0.01$).

Model Adequacy Evaluation

The model has a high explanatory power as the value of R-squared is 0.8815 which indicates that the exposure variables explain about 88 percent of the variation in the return on assets (ROA). The Wald test value of 422.29 ($p = 0.0000$) proves the significance of the model in general. The diagnostic tests show that there was no problem with the specification of the model. The Friedman test value of 6.818 ($p = 0.448$) shows that there is no interdependence across cross-section (no correlation in the residuals across the firms). Jochmans Portmanteau of 8.000 ($p = 0.998$) does not indicate any autocorrelation, which means that the residuals are not correlated over a long period of time.

Discussions and Contributions

The empirical results indicate that the financing pattern adopted by the consumer goods firms in Nigeria is more likely to follow the Pecking Order Theory in which the preference is put on debt financing rather than equity financing. It appeared that equity ratio has negative effects on ROA because companies that depend on equity financing have poor financial performance which may be as a result of the high costs involved in equity issuance. On the other hand, the opportunity effect of debt ratio on ROA indicates that debt leverage is a positive effect of performance in firms probably because of tax advantages and discipline as a result of having debt to service. The findings are in line with the works of other researchers such as Babalola et al. (2022), Sani et al. (2019), Nestor and Chijioke (2023), and Oke and Fadaka (2021) who also reported the existence of such relationships between capital structure and the performance of firms in Nigeria. What the findings suggest is that companies need to focus on debt financing rather than equity to increase performance though not to the point of over-leveraging. Bigger companies will be more effective and it shows that there will be economies of scale. Additionally, companies ought to make the best use of their capital structure and use debt financing as a way of improving performance. Equity financing must be done sparingly bearing in mind that it affects ROA negatively.

The study adds to the existing empirical literature on the interaction of capital structure and firm's performance in Nigerian manufacturing sector. It affirmed to the fact that the financial performance of consumer goods industry in Nigeria market condition does not solely rely on the way the capital is been structured.

Limitations and Suggestions for future Studies

The sample size of eight firms and duration of ten years is longer than the one utilized by most of the previous studies, this scope is still acknowledged as a limitation to attaining better outcome for the study. It therefore suggested that researchers in the future should extend the scope in terms of number of firms and longer data horizon. In addition, the study scope in terms of sector should be extended to sectors like communication and automobile sectors which have not been consider on this subject.

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