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"The Role of Financial Structure in Determining Profitability of Firm in Pakistan"

By:

Minahil Mahmood Bhatti ***01-321251-043***

Supervisor:

Mr. Tanveer Taj

HR and Management Department

Bahria Business school

Bahria University Islamabad

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Names of Student: Minahil Mahmood Bhatti Enroll # 01-321251-043

Class: MBA 1.5

Approved by:

_____

Mr. Tanveer Taj

Supervisor

_____

Qurat Ul Ain Waqar

Research Coordinator

_____

Dr. Aftab Haider

Head of Department

ABSTRACT

Financial structure is a key determinant of firm profitability, particularly in emerging economies where firms operate under changing economic and market conditions. Financial structure plays a critical role in determining firm profitability, particularly in emerging economies such as Pakistan. While previous studies have primarily examined firm-level financing decisions, limited research has explored the combined effects of firm-level financial structure, sector-specific characteristics, and macroeconomic factors on profitability. This study addresses this gap by investigating the impact of financial structure on the profitability of non-financial firms listed on the Pakistan Stock Exchange (PSX). A quantitative research design was employed using secondary panel data from 10 firms across five sectors (textile, cement, chemical, energy, and sugar) covering the period 2005–2024. Profitability was measured using Return on Assets (ROA), Return on Equity (ROE), and Earnings per Share (EPS), while descriptive statistics, correlation analysis, and multiple regression analysis were used for data analysis. The findings reveal that retained earnings positively and significantly influence profitability, whereas short-term debt and shareholders' equity have significant negative effects, and long-term debt shows no significant impact. Interest rates and Inflation rates exhibit a negative effect on profitability. The study concludes that firm profitability is jointly influenced by financing decisions, sector characteristics, and macroeconomic conditions, and recommends optimizing capital structure and incorporating economic conditions into financial decision-making to enhance long-term profitability.

Keywords: Financial Structure; Capital Structure; Profitability; Retained Earnings; Short-Term Debt; Long-Term Debt; Shareholders' Equity; Pakistan Stock Exchange; Non-Financial Firms; Panel Data.

JEL Classification Codes: G32 (Financing Policy; Capital and Ownership Structure), G30 (Corporate Finance and Governance: General), L25 (Firm Performance: Size, Diversification, and Scope), C23 (Panel Data Models), O16 (Financial Markets and Economic Development).

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