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"Impact of Operating Leverage, Liquidity, and Profitability on Stock Returns: Evidence from Non-Financial Firms Listed on PSX."

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Abstract

In this study the stock returns of non-financial companies trading on Pakistan Stock Exchange have been analyzed and the association between operating leverage, liquidity, profitability, financial leverage and size of the firm has been examined. The primary goal of the research was to explore and explain the factors of the firm that affect stock returns. The value of stock returns is important, because they influence investment decisions, firm valuations, financing decisions and market efficiency.

The research conducted a literature review and literature synthesis covering the previous literature that is relevant to the study to obtain a glimpse of what factors are influencing the return behavior of stocks. In order to establish a broad theoretical base for the study, a thorough review of literature was conducted, involving pertinent studies on the determinants of capital structure, profitability, liquidity and the performance of the stock market. Data from 689 observations of 53 non-financial firms over 13 years were analyzed with panel data techniques. To choose the best estimation model, descriptive statistics, correlation analysis, Fixed Effects Model, Random Effects Model and Hausman Test are used. SPSS and STATA software were used to analyse the statistics.

The results indicated that profitability and leverage significantly and positively affected stock returns whereas operating leverage, liquidity, and size did not. The results suggested that among the variables examined the profitability was the most influential factor for stock returns. The authors suggest that additional variables at the macroeconomic and the firm-specific levels be introduced into the study in the future to get a comprehensive understanding of stock return behavior. In addition, companies need to pursue higher profitability and sound debt leverage management in order to add value for shareholders.

keywords: Stock Returns, Operating Leverage, Liquidity, Profitability, Financial Leverage, Firm Size.

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