

The capital structure adjustment through debt financing based on various macroeconomic conditions in Korean market*

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Abstract

We investigate the relationship between the capital structure and the economic conditions in Korean market. To find the adjustment behavior on capital structure depending on macroeconomic conditions, we use dynamic partial adjustment model to estimate adjustment speeds toward targets. As the data analyzed in the study, we use non-financial firms listed in the Korean stock exchange. Through the empirical test, we find evidence that is consistent with Hackbarth, Miao and Morellec (2006) and Cook and Tang (2010)'s arguments that firms tend to adjust faster their leverage toward target level in economic expansion. Thus, our findings support to the pecking order and market timing theories in terms of corporate finance theories on capital structure. In addition, our test results are re-confirmed with robust consistency even though we include year dummy variable in the empirical test model for controlling global financial crisis in contrast with Kim (2013).

Key words: adjustment behavior, macroeconomic conditions, dynamic partial adjustment model, pecking order and market timing theories.

JEL Classification: G3.

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Resumen

En este trabajo investigamos la relación entre la estructura de capital y las condiciones económicas en el mercado coreano. Para conocer el comportamiento de ajuste de la estructura de capital respecto a las condiciones macroeconómicas, utilizamos un modelo de ajuste parcial dinámico que estima las velocidades de ajuste hacia los objetivos. Los datos analizados en el estudio corresponden a las empresas no financieras que cotizan en la bolsa de valores de Corea. Empíricamente encontramos evidencia que es consistente con los argumentos de Hackbarth, Miao y Morellec (2006) y Cook y Tang (2010), respecto a que las empresas tienden a ajustar más rápidamente su apalancamiento respecto al nivel objetivo durante la expansión económica. Por lo tanto, nuestros resultados apoyan las teorías de *pecking order* y de *market timing* en términos de las teorías de finanzas corporativas relativas a la estructura de capital. Además, los resultados de nuestras pruebas son consistentemente robustos a pesar de que incluimos en nuestro modelo una variable ficticia ligada al tiempo como mecanismo de control de la crisis financiera global, en contraste con Kim (2013).

Palabras clave: comportamiento de ajuste, condiciones macroeconómicas, modelo dinámico de ajuste parcial, teorías de *pecking order* y de *market timing*.

INTRODUCTION

Korajczyk and Levy (2003) have suggested target capital structure as the function of economic conditions and firm characteristics. Based on the results from Korajczyk and Levy (2003), we postulate that economic conditions have a significant effect on debt and equity issuance in firms with financial constraints rather than in firms without financial constraints. Thus, we infer that economic conditions and a firm's characteristics may result in variability, and that also this variability differentially affects capital structure. Even though there are some studies on the relationship between security issuing and economic condition like Hackbarth, Miao and Morellec (2006) and Cook and Tang (2010) for North America firms, it is hard to find the previous studies analyzed with the sample data of Korean firms.

Especially, Korea is one of core countries among many emerging countries and we think that the empirical result on Korean firms plays a benchmark role in inferring from the debt financing behavior of other emerging countries. As the reason why we study on Korean firms' debt financing behavior, we can suggest that Korean firms have experienced rapidly growth and undergone bailout for Asian financial crisis in 1997 as a typical economic cataclysm case to understand the mechanism between debt financing behavior and economic condition.

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