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Global Leverage Adjustments, Uncertainty, and Country Institutional Strength*Gonul Colak^a, Ali Gungoraydinoglu^b, and Özde Öztekin^c

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Abstract

Using a broad range of uncertainty measures, we show that uncertainty dramatically slows down firms' adjustments toward their optimal capital structure. At the upper bound, the estimated speed of leverage adjustments almost halves when uncertainty is high. High quality institutions (common law legal origin, more disclosure to congress and/or to the public, and higher public sector ethics) and presidential political systems offset some of the adverse effects of uncertainty on leverage adjustments. The financial crisis has altered the relationships among uncertainty, adjustment speeds, and a country's institutions; more so for countries with weak institutions and parliamentary systems.

JEL classification: G30; G32; G35

Keywords: Institutions; International; Leverage; Uncertainty; Speed of Adjustment; Financial Crisis

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