Liquidity and capital structure: A case of Thailand

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ABSTRACT

This paper contributes to the capital structure literature by analyzing the relationship between liquidity and capital structure for of 101 Thai firms listed on the Stock Exchange of Thailand. Both univariate analysis and panel regressions analysis are performed for the period 2002-2008. Three liquidity measures, which are the Amihud estimate, modified turnover, and modified liquidity ratio, are employed as proxies for liquidity in this paper. It is found that liquidity is negatively correlated with leverage. Specifically, the sign of this relationship suggests that firms, with more liquid stocks, tend to prefer equity financing to debt financing when raising external capital. The results are robust to each of the three liquidity measures employed in this paper. In addition, the results remain the same either when random effects model or firm-specific fixed effects model is performed as the alternative specification. Moreover, the results are consistent with previous literatures in which higher stock market liquidity lowers the cost of equity. Therefore, a higher level of equity financing is expected for firms with more liquid stocks. Besides, the results highlight the effects of liquidity on corporate financing decisions of firms in Thailand.