



Applied Economics >

Volume 48, 2016 - Issue 5

540 | 16 | 1  
Views | CrossRef citations to date | Altmetric

Original Articles

# Mean reverting financial leverage: theory and evidence from Pakistan

Tanveer Ahsan, Wang Man & Muhammad Azeem Qureshi

Pages 379-388 | Published online: 11 Sep 2015

Cite this article <https://doi.org/10.1080/00036846.2015.1080802>

Check for updates

Sample our  
Economics, Finance,  
Business & Industry Journals  
>> [Sign in here](#) to start your access  
to the latest two volumes for 14 days

Full Article

Figures & data

References

Citations

Metrics

Reprints & Permissions

Read this article

Share

## Abstract

Grounding concepts of the two competing theories of capital structure (trade-off theory, pecking order theory) are quite opposite to each other. Trade-off theory claims that there is an optimal (target) capital structure and firms try to achieve that optimal (target) point. Whereas pecking order theory argues that there is no optimal (target) capital structure but the firms follow a specific pattern of financing. Using the two competing theoretic frameworks, this study applies Fisher-type panel unit root test to an unbalanced panel data of 13 115 firm-year observations of nonfinancial firms listed on Karachi Stock Exchange Pakistan spread over 38 years (1973–2010). Overall panel test results, for short-term, long-term, as well as total leverage support trade-off financing behaviour while individual firm results do not. Individual firm results show that only 16% of the firms have short-term target, 25% of the firms have long-term target and 12% of the firms have total target leverage ratio. Further, industry results

explain that most of the industries do have target leverage ratios and classification of data into profitable and lossmaking firm-year observations explains that profitable firms clearly follow trade-off financing behaviour while the results for lossmaking firms do not support trade-off financing behaviour. Our study indicates that it is important for the government to ensure policies to develop well-balanced financial markets and to improve accountability systems.

#### KEYWORDS:

Target capital structure    Pakistan    unit root analysis    panel data

#### JEL Classification:

C23    G30    G32

#### ORCID

Muhammad Azeem Qureshi  <http://orcid.org/0000-0001-5107-2192>

#### Notes

<sup>1</sup> <http://www.sbp.org.pk/ecodata/NPL.pdf> of State Bank of Pakistan reports PKR 594 billion (approximately US\$ 7 billion) as nonperforming loans of banking sector in Pakistan. Apex court of Pakistan is currently hearing a case in this regard.

#### Related research

People also read

Recommended articles

Cited by  
16

## Information for

Authors

R&D professionals

Editors

Librarians

Societies

## Opportunities

Reprints and e-prints

Advertising solutions

Accelerated publication

Corporate access solutions

## Open access

Overview

Open journals

Open Select

Dove Medical Press

F1000Research

## Help and information

Help and contact

Newsroom

All journals

Books

## Keep up to date

Register to receive personalised research and resources  
by email

 Sign me up

  

  

Copyright © 2026 Informa UK Limited Privacy policy Cookies Terms & conditions

Accessibility

 Taylor and Francis Group

Registered in England & Wales No. 01072954  
5 Howick Place | London | SW1P 1WG