



NEAR EAST UNIVERSITY
GRADUATE SCHOOL OF SOCIAL SCIENCES
BANKING AND ACCOUNTING PROGRAM

**THE IMPACT OF CAPITAL STRUCTURE ON FINANCIAL
PERFORMANCE OF COMMERCIAL BANKS IN JORDAN**

RAAD ALSAKARNEH

MASTER'S THESIS

NICOSIA

2018

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THESIS SUPERVISOR
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NICOSIA
2018

ACCEPTANCE

We as the jury members certify the “**The impacts of capital structure on financial performance of commercial banks in Jordan**”

Prepared by Raad Alsakarneh defended on

31th May 2018

**Has been found satisfactory for the award of degree of
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DECLARATION

I am Raad Alsakarneh , hereby declare that this dissertation entitled “The impact of capital structure on financial performance of commercial banks in Jordan” has been prepared myself under the guidance and supervision of “**Assoc. Prof. Dr. Turgut Türsoy**” in partial fulfilment of The Near East University, Graduate School of Social Sciences regulations and does not to the best of my knowledge breach any Law of Copyrights and has been tested for plagiarism and a copy of the result can be found in the Thesis.

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DEDICATION

I must express my very profound gratitude to my parents and to my close friend Othman Shnaikat for providing me with unfailing support and continuous encouragement throughout my years of study and through the process of researching and writing this thesis. This accomplishment would not have been possible without them. Thank you.

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ABSTRACT

THE IMPACT OF CAPITAL STRUCTURE ON FINANCIAL PERFORMANCE OF COMMERCIAL BANKS IN JORDAN

This Study investigated the effect of capital structure on financial performance of 6 commercial banks in Jordan for the 17 year period from 1999-2016. The two proxies that measure bank performance use in the study is Return of Assets (ROA) and Return on Equity (ROE). Five explanatory bank variables which are each banks' debt ratio, liquidity adequacy ratio, loan deposit ratio, total assets and equity to total assets ratio were regressed against each of two performance indicators.

In order to achieve the objectives of the study, a statistical package E-Views was used to model variables through a Panel Least Square method. The results of the study shows that equity to assets ratio is positively related to ROA while high debt ratio results in low or negative ROA. Low bank Liquidity, high loan to debt ratio and bank size affects ROA negatively. The ROE models shows that Debt ratio, equity to asset ratio, equity to assets ratio and loan deposit ratio affects Return on Equity negatively or does not result in full capacity utilization of assets amongst Jordan banks. The bigger the bank size the higher the return o assets. Recommendations are that Jordan banks has to increase the equity to assets ratio in order gain full capacity utilization of assets and to maximize shareholder value banks has to grow their asset base.

Keywords :(capital structure, financial performance, commercial banks)

ÖZ

SERMAYE YAPISININ ÜRDÜN'DEKİ TİCARİ BANKALARIN FİNANSAL PERFORMANSI ÜZERİNDEKİ ETKİLERİ

1999-2016 seneleri arasında Ürdün'deki ticari bankalarının sermaye yapılarının finansal performansları üzerindeki etkileri incelenmiştir. Araştırmada banka performansını ölçen iki unsurdan biri Aktif Karlılık ve ikincisinde Özsermaye Karlılık oranlarıdır. Beş adet açıklayıcı banka değişkenleri, her bankanın borç oranlarını, likite yeterlilik oranlarını, kredi mevduat oranlarını, toplam varlıklarını ve öz kaynak-toplam varlıklar oranlarını iki performans unsurlarına indirgenmiştir.

Araştırmanın hedeflerini tutturabilmek için istatistiksel paket E-Views kullanılarak Panel Least Square yöntemi ile değişkenler biçimlendirilmiştir. Araştırmanın sonuçları öz kaynak-toplam varlıklar oranının olumlu şekilde Aktif Karlılık'a bağlı olduğunu, başka bir yandan ise yüksek borç oranının düşük veya olumsuz Aktif Karlılı'a neden olduğu sonucunu bulmuştur. Düşük banka likitelik oranı, yüksek borç-kredi oranının ve banka büyüklüğünün Aktif Karlılık'ı olumsuz etkilemektedir. Özsermaye Karlılık modeli, borç oranının, öz kaynak-toplam varlıklar oranlarının ve kredi mevduat oranlarının Özsermaye Karlılık üzerinde etkisinin olumsuz olduğunu veya Ürdün bankalarında tam kapasitesiyle varlıklarını değerlendirmediğini göstermiştir. Banka ne kadar büyük olursa varlılığa olan dönüş o kadar artıyor. Ürdün banlarının öz kaynak-varlıklar oranını artırarak tam kapasitesiyle varlıkların değerlendirme olanığının oluşturmaları ve hissedar değerinin azami seviyeye çıkarılması için verilen tavsiyedir.

Anahtar Kelimeler: (sermaye yapısı , finansal performans, ticari bankalar)

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ABBREVIATIONS

ADF:	Augmented Dicky Fuller tests
EAR:	Equity to Asset Ratio
EBITD:	Earnings before Interest Tax and Depreciation
GDP:	Gross Domestic Product
LAR:	Liability to Total Asset Ratio
NIM:	Net Interest Margin
NPV:	Net Present Value
PER:	Profit to Expense Ratio
PLS:	Panel Least Square method
ROA:	Return on Assets
ROD:	Return on Deposits
ROE:	Return on Equity

INTRODUCTION

Capital structure is normally related to how well the business is financed in terms of capital provided by either shareholders or equity holders (Maina, 2014). In any business enterprise, capital structure serves as important purpose as it ensures that funds are readily available to meet operational demands. For instance, a study by Gleason et al. (2000), indicated that capital structure is used to absorb losses incurred by the business while a study by Saunders and Cornett (2003) indicated that capital structure is a representation of the ability of the firm to meet unforeseeable risks. But in most cases capital structure has been highly linked to size with ideas pointing to the fact that big firms have high capital structure (De Mesquita and Lara, 2003; Velnampy and Niresh, 2012). Meanwhile, it is imperative that firms have adequate capital structure to support their operations and their possible plans to expand market operations and growth in size. This is supported by the idea that in order to grow bigger, firms must have the capital structure that allows them to venture into new products and markets (Yat et al., 2002). Alternatively, capital structure is also an internal method that firms can use to gain a competitive advantage over their competitors (El-Sayed, 2009). This is because firms with high capital structure can easily respond to market and industry opportunities and threats (Shubita and Alsawalhah, 2012). Alternatively, capital structure can also be used to finance research and development activities which are of huge important to the firm as they facilitate innovation and technological developments that foster effectiveness and efficiency in business operations (Abor, 2005; Cornett, 2003; Maina, 2014).

The relationship between capital structure and capital structure is usually tied to what capital structure can able to do for the business. This stems from idea that shows that capital structure allows firms to invest in profitable projects and assets which have a tendency to generate high returns in the future (Gleason et al., 2000; Saunders and Cornett, 2003). Increases in financial performance as a result of improvements in

capital structure are sometimes caused by major improvements in operations, production and, product and service delivery (Rao et al., 2007). This is made possible through innovative investments in research and development activities (Pratheepkanth, 2011). Thus firms will make more profits which lead to positive in financial performance as reduction in costs, wastage and limitation is made from the introduction of new and better production and service methods (Nirajini and Priya, 2013). The financial performance of firms such as banks is highly related in their capital structure positions and banks with a high capital structure are usually quite able to withstand losses and risks (El-Sayed, 2009). Such as ability to absorb losses is what keeps them afloat and cushion their financial performance. From this introductory insights about the influence of capital structure on financial performance of firms, it can therefore be noted that capital structure has a high tendency to influence the financial position of firms.

Believes are high among academic scholars that a better capital structure allows firms such as banks to be capable of investing in profitable projects and assets that will generate high future returns (Abor, 2005; Gill et al., 2002; Velnampy and Nireesh, 2012). This in turn results in an increase in financial performance as the profitable projects and assets begin to generate an inflow of high returns (El-Sayed, 2009; Nirajini and Priya, 2013; Pratheepkanth, 2011). Thus the impact of capital structure on financial performance has been deemed to be positive (Saunders & Cornett, 2003; Shubita and Alsawalhah, 2012) But observations have been made positive changes in capital structure do not always lead to improvements in the financial position of firms (De Mesquita, 2003; Yat et al., 2002). For instance, a study by Maina, (2014) posits that that capital structure that is highly dominated by debt equity has an adverse effect on financial performance. Moreover, the impact of capital structure is considered to be in determinant in most cases. This is because a study by Cornett (2003), highlighted that there are a lot of factors that influence the relationship between capital structure and financial performance. Hence, the relationship is not always positive and it can be negative or in some cases significant and in others insignificant. Furthermore, it cannot be easily determined how capital structure will influence the financial performance of

firms in Jordan especially banks which have been subject to a lot of capital structure reforms. This therefore shows that it remains unclear as to the exact impact capital structure will pose on the financial performance of firms especially banks in Jordan. This study therefore seeks to examine the impact of capital structure on financial performance of firms in Jordan.

This study attempts to examine how capital structure influences the financial performance of firms in Jordan. The study also seeks to achieve the following aims;

- To determine possible capital structure limitations encountered by firms in Jordan?
- To examine how capital structure limitations encountered by firms in Jordan affect their financial performance?
- To determine possible corporate strategies that can be used to improve the financial performance of firms in Jordan?

With respect to the above given objectives, the undermentioned questions can be developed and this study therefore seeks to offer answers to these questions.

- How will capital structure influence a change in financial performance?
- What are the possible capital structure limitations encountered by firms in Jordan?
- How do capital structure limitations being faced by firms in Jordan affect their financial performance?
- What are the possible corporate strategies that can be used to improve the financial performance of firms in Jordan?

Significance of the study It can be noted that firms with high and good capital structures have a greater ability to withstand economic and business hardships. Hence by

offering suggestions on measures that can be adopted to boost capital structure levels, firms will be capable of surviving economic and business difficulties that threaten their survival and growth. This study also offers a series of corporate strategies that can be used to improve financial performance of firms not only in Jordan but also around the world. The undertaking of this study also helps in making academic improvements in future empirical studies.

This study is composed of five chapters as outlined as follows;

- Introduction
- **Chapter one:** Literature review and Overview of capital structure and financial performance of banks in Jordan
- **Chapter two:** Research methodology
- **Chapter three:** Data analysis and presentation.
- **Chapter four:** Conclusions, recommendations and suggestions for future studies

1. CHAPTER: LITERATURE REVIEW

1.1 CAPITAL STRUCTURE AN OVERVIEW

Capital Structure concept draw much consideration subsequently to Modigliani and Miller (1958), sit-in in one of their papers that the selection amidst DE has a trivial effect on the value of the organisation. This suggestion surely does hold veracious assuming a perfect capital market. Defined a perfect market is such where they are no frictions the likes of bankruptcy and transaction cost. As a result of related business transactions costs and expenditure such perfect markets are no longer in existence. Additionally practically other market participants have easier and faster access to information than others such that at any particular point in time they can make more informed market decision than the other participants. In this respect the relevance of capital cost is brought about by the existence of such imperfections in markets. As postulated by Strabulaev (2007:1787), minor adjustment costs might result in larger differential in capital structure.

Inconsistence with the researchers after their research in 1958, resulted in Modigliani and Miller (1963) to alter the original capital structure insignificance suggestion for excises. As interest on borrowings is a tax-deductible expenditure the organisation economically lowers its tax obligation by signing up for extra borrowings. An increase in the debt to equity ratio also result in an increase in the market value of the firm by the present value of the interest shield. The implication of this is that the cost of capital will not increase, even if the use of leverage increase to excessive levels. According to Solomon (1963:276), in an utmost leverage situation, the interest must increase. Due to the fact that extreme points of liabilities prompt marketplaces to respond through requesting increased return rates. Thus, to abate the WACC, organizations evades an untainted credit situations thus pursuing a balanced portfolio of borrowings and equity. In an observation done in 1970s by Kim (1978:45), it was clarified that non finance organizations in the USA were financed by just a third of borrowed funds. Such discovery offers elaborate evidence which is in the existence of taxes, companies dodges untainted credit situation.

Two justification exist for reduced borrowing levels in levered firms (Baxter, 1967:395). The first is that rate of interest on borrowings might be directly linked DR ratio. The implication being that as an organisation increases its debt levels, the lenders will ask

for a higher return rate on the debt. The second is that higher borrowing levels makes it probable for interest payments defaults, in so doing leading to bankruptcy. As a result organisations strives for a mix of funding that maximise the tax rebates which are a resultant of extreme credit positions and additionally lessening chances of insolvency. A number of researches have nonetheless, proved the presence of an optimal debt to equity mix. The sole basis being the presences of imperfect markets conditions the likes of transactions costs etc. An epitome is a substantiation through indifference curves that the introduction of transaction costs to the value irrelevance equation bring about a disequilibrium, where the stockholders strive for an optimal level in the mix of debt and equity (Baumol and Malkiel, 1967:554).

A couple of years after the fact, Stiglitz (1972) acknowledged the ramifications of insolvency on the estimation of the organisations and contends which is beneath specific suppositions, inexistence is ideal capital structure. Such contention hinges on premise that without liquidation, nominal rates on obligation are free of DR proportion. Nonetheless, if probability for liquidation exist, the nominal fees on the credit increases, in this manner rendering securities to be more unsafe. Hence, the market estimation of the firm will rely upon the likelihood of liquidation, regardless of whether exchange expenditure were disregarded.

Kraus et al (1973) present commercial duties and insolvency punishments into a government inclination model of ideal monetary arrangement, and affirmed was the presence of a perfect capital arrangement. Turnbull (1979) in agreement demonstrates that perfect capital organisation of an esteem amplifying company happens prior to firms obligation limit. This is the most extreme measure of credit which might be stretched out by providers of funds. Also, Brennan et al (1978) contend that likelihood of insolvency costs expands vulnerability of forthcoming expense investment funds, and showed that such vulnerability is adequate for instigation of an ideal capital structure, regardless of whether insolvency expenditure are disengaged from the model.

As per Miller (1988), capital structure superfluity recommendation was not planned to propose that DR value proportion was vague. With this, Myers (2001) exhorts that the Modigliani and Miller (1958) suggestions ought to be seen as a benchmark, and not

the perfect final product. The recommendations are just demonstrating that financing does not make a difference, with the exception of particular exchange costs.

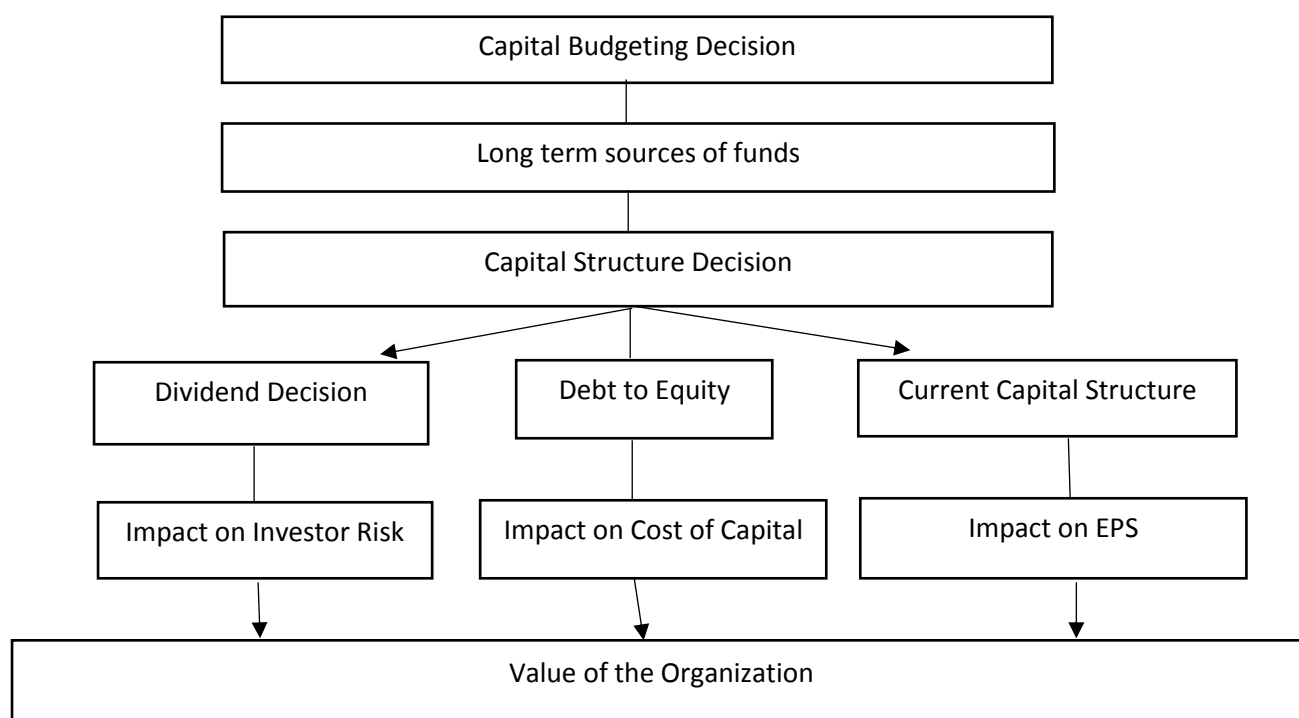
Capital Structure of an organisation basically entails the model with which firm is financed. The decision of the model of capital structure is a vital decision if the firm is to manage its finances well. The chief objective of the capital structure decision be aimed at ensuring maximisation of shareholders wealth or the ultimate value of the firm. Value of the firm hinges on anticipated earning and cost of the finances. The capital structure impacts the value of the organisation by operating on either anticipated returns or the value of the capital or both. As a result of the deductibility of the tax expenses on interest payment, being highly leveraged on surfaces reduces the tax liability of an organisation, however it does enhance the financial risk of the firm.

Consequentially management ought to select the model of capital structure in which the level of debt minimize the entire capital cost, maximizes the returns left for the equity holders hence maximizing the overall value of the organisation . The need to stick a balance on capital structure bring the concept of optimal capital.

Determinants of Capital Structure

- 1) Risk Minimization
 - The structure of the capital have to be in tandem with the entire business risk.
 - Also the resultant should be particular level of financial risk.
- 2) Control: The structure of the capital unveil the managements take on the control of the organisation
- 3) Flexibility: Implies the extent to which the organisation can meet the requests of the ever dynamic environment.
- 4) Financial Performance: The structure has to enhance the financial performance of the firm from the perspective of the owners of the firm.
- 5) Solvency: Extra ordinary debt utilization put a risk the solvency of the firm.

Capital Structure Decision Process



1.2 Overview of Jordan Banking Sector

Despite the fact that the banking and insurance division is one of the littlest budgetary frameworks in the area, it is considered as a standout amongst the most vital segments of the economy of Jordan, adding to around 11.6% of Gross Domestic Product (GDP) at consistent costs in 2011. Be that as it may, the economic significance of the Jordanian banking sector isn't just showed by its critical commitment to Gross domestic product, as it is additionally considered as one of greatest employers inside the private segment and has the biggest capitalization of the Amman Stock Exchange, which makes it a key column and a principle driver of the Jordanian economy.

The sector has been developing as of late and this development is reflected by the noteworthy ascent in the aggregate resources of authorized banks which more than trebled in estimate from JOD 14.15 billion in resources in 2000 to JOD 60.5 billion toward the finish of development rate of 328% (implying that banks' aggregate resources dramatically multiplied amid this period). This development is credited to the fairly traditionalist banking policies embraced by banks in Jordan that empowered the nation to withstand the worldwide financial crisis in 2009.

Jordan's banking sector is thought to be well developed by provincial principles with various organizations, speculation, and retail benefit offerings. The Jordanian banking segment is mindfully overseen and successfully regulated by the Central Bank of Jordan (CBJ), and this approach of banking system framework administration has brought about an arrangement of good macro-prudential indicators, proven resilient to domestic and external shocks over the last few years, such as the global financial crises in 2009 and the what is referred to as the 'Arab Spring' in some countries of the region, maintaining its expansion and growth during 2013, and Jordanian banks are already well on the way to satisfying major components of Basel III regarding capital adequacy and liquidity. Both local and international banks are operational and growing in Jordan. Whereas, the Amman Stock Exchange is modern and enjoys no taxes on capital gains, no taxes on cash dividends, free repatriation of investment and income, no ceiling on foreign equity ownership and privatization.

The Jordanian banking sector is all around capitalized. While the capital sufficiency proportion required by the Basel II Accord is 8%, the CBJ prerequisite is 12%, banks in Jordan are promoted at 19.2%, and have been reliably outperforming the CBJ necessity throughout the most recent 10 years, achieving a low of 15.9% of every 2003 and a high of 21.4% out of 2006. The Jordanian banking sector is likewise gainful. Profits for value of almost 14% likewise demonstrate the proceeding with gainfulness of this area. As per the International Monetary Fund, be that as it may, the nation suffered a "credit mash" amid the financial crisis inferable from fixed credit conditions. Traditionally, the vast majority of banking activity has centred on the capital city of Amman and other regions have been less well-banked.

1.2.1 Overview of the Six Banks under Study

1.2.1.1 Jordan Kuwait bank

Jordan Kuwait Bank, a Jordanian public shareholding company, was founded in 1976 and has magnificently progressed into a major player in the Jordanian banking sector over the last few decades. The bank currently operates a domestic network of 62 branches and offices distributed throughout Jordan in addition to four branches in Palestine and a branch (IBU) in Cyprus. The bank's paid-up capital was gradually increased from JD 5 million in 1976 to JD 100 million (USD 141m) in 2008. Basing on the bank's website, its philosophy rests on the concept of bringing capital into Jordan from other Arab countries, especially Kuwait

1.2.1.2 Bank of Jordan

The Bank of Jordan is a bank in Jordan, and it holds the second position on the size of the financial institutes in the country .It was commenced operations in 1960 and is based in Amman. The Bank of Jordan offers credit cards and Internet banking. It operates over 100 bank branches in Jordan and 12 branches in the West Bank and Gaza Strip areas, and over 150 machines. The bank's stock is listed on the Amman Stock Exchange's ASE Weighted Index.

1.2.1.3 The Housing Bank for Trade and Finance

The Housing Bank for Trade and Finance (HBTF) was established in 1973 as a public shareholding limited company with a capital amounting to half a million JD. The primary focus of the Bank was to provide housing finance, and hence the name.

1.2.1.4 Cairo Amman Bank

The bank was incorporated in 1960 as a Jordanian public shareholding company and commence its services on the 1st of July 1960. The Cairo Amman Bank is a full-benefit

bank in Jordan and Palestine, with head office in Amman. The head office toward the Palestinian regions is in Ramallah. The bank works around 84 branches and workplaces in Jordan and 21 in the Palestinian domains. CAB right now positions 6th in Jordan and third in the Palestinian regions in light of benefits. It is additionally positioned third in the Palestinian domains in light of the quantity of branches it has. The bank is an individual from the Jonet ATM organize in Jordan.

1.2.1.5 Arab bank

Arab Bank is one of the biggest financial institutions in the Middle East, established in 1930 in Jerusalem, Mandatory Palestine, as the principal private division financial institution in the Arab world. Headquartered today in Amman, Jordan, it serves customers in excess of 600 branches spreading over five mainlands. Arab Bank is an openly held shareholding organization recorded on the Amman Stock Exchange. Jordan national bank

1.2.1.6 Jordan National Bank

It is of Jordan originality incorporated in 1955 and has its HQ in Amman. The bank hold a sixth position in terms of public shareholding establishment in Jordan.

1.3 Bank profitability Theories

It is inevitable for researchers to agree to the notion that commercial banks are of greater importance in the financial industry as well as to the economy. For this reason it is worth mentioning that commercial banks, over the years have contributed immensely to economic development. Since banks do distribute financial resources around the economy, transferring savings into borrowing and so on this is made possible. Equitable distribution of financial resources, development of economies and expansion of industries and firms are all tied to favourable performance of banks.

Thus banks are key to economically development, and not just to the financial industry. Financial performance through profitability assess performance of banks, taking into consideration their operational environment. According to Goddard et al. (2004), in order to withstand the soundness of the financial sector and improve economic and financial industry, profitability of commercial banks is critical. As a result financial

performance of banks has been a widely researched topic of late. Studies on financial performance of banks via analysis of bank profitability started in 1970s, proceeding to 1980s in the form of implementation of profitability models or theories such as the Efficiency and Market Power models Athanasoglou et al. (2006). Another model was put across to add on to the existing model on profitability of financial institutes that is the balanced portfolio model, Nzongang and Atemnkeng (2006).

1.3.1 Market Power theories

Under this model financial performance of banks is subject to the market arrangements if the industry, Tregenna (2009). Two different models are housed in the exchange influence model: the SCP RMP theory. The level of market saturation a particular bank is functional in is of significance, since the more saturated the market is the more competitive that particular market is, this in line with the SCP method. When a bank manages to out compete its counterparts it creates for itself a monopolistic environment hence earning more profits, (Tregenna, 2009).'

Bourke et al. (1989) attested that a favourable connection is found amid bank financial performance and the level of bank concentration as increased market power result in monopolistic advantages. Additionally on this note collusion premise is seen as in agreement to the market power theory meaning it is of the same notion that a positive relationship exist between market saturation and bank profitability performance. As per this theory merger of small number of banks is possible whether willing or otherwise. Such mergers might disrupt the market leading to expensive loans for households and other individuals. However for this to work the issue of small number of banks have to prevail otherwise the collusion becomes difficult, Goddard et al. (2004).

On the other hand the RMP model, says that the percentage of the market as compared to the total industry market share a particular bank controls have an influence of the gains which accrues to it. Financial institutions which offer differentiated products stand a chance to control a sizeable percentage of the market share (Tregenna, 2009). Similarly the ES hypothesis confirms firms with administration with vast know-how or else modern expertise experience less loss and inevitably improved profits. The firms equally assumed to achieve greater market shares, which

necessarily might increase firm concentration, essentially as exceptionally saturated marketplaces will lower the costs of collusion (Demsetz, 1973, Smirlock, 1985). Unsurprisingly, collusion of firms have positive impact on financial performance.

Also market share is midst the chief external factors that influence bank financial performance; since every industry have competition forces that are peculiar to that sector and such variables have an influence on the financial performance. Hence corporations that function in highly competitive industry infrequently attain encouraging earnings on their processes. Smith (1984) states that stiff rivalry amid commercial banking industry tends to diminish profitability. The microeconomic theory suggests that commercial sector which function in an oligopolistic situations tends to cause a hostile rivalry for sophisticated market development level hence without doubt influence the profitability of the corporate sector.

1.3.2 Efficiency Theory

How efficient a firm is determines how profitable it becomes that is the more efficient a bank is the more profitable it must be *ceteris paribus*. Just like the market power theory, this theory as well is dichotomized into: the X-efficiency and Scale-efficiency assumption. As a result of X-efficient, efficient firm's profitability performance is vibrant because of lowered costs. Moreover, the scale approach stress on scale economies as equated to variations in administration or production expertise. Due to scale economies larger organisations can attain reduced unit cost hence enhanced profits. Inevitably organisations which enjoys scale economies control a larger portion of the market share since they will be big enough to draw economies of scale, Athanasoglou et al. (2006). Suffice to say connection exist amid SCP and SE.

1.3.3 The Balanced Portfolio theory

Mentioned to be one of the chief paramount theory of bank performance studies, Nzongang and Atemnkeng (2006). In association to the theory the greatest valuable beneficiary is through an element of method selections categorised by several variables. Agreed was the capability to rise great earnings be contingent on the appropriate prearrangement of properties including debt organised with the assistance

of executives and cost per unit assimilated by the financial institution for bringing a share of the resources.

1.3.4 The Risk-return trade off theory, the signaling and insolvency cost theory

Balance sheet structure of a bank can as well have influence of the financial performance of banks; accordingly the capital to assets-ratio is a crucial balance sheet ratio. According to Modigliani and Miller (1958) attest that no connection subsists amid the capital structure and prevailing value of the financial institution. As per the hypothesis, increasing risks, through rising control and reducing capital to resources proportion is consequential to greater estimated earnings as organisations are keen to partake additional peril if expected revenue may rise. Ommeren (2011) defined this theoretical amplification the risk-return trade off. However theoretical elucidations occur which is a greater capital to assets proportion have positive influence profitability. According to Berger (1995), these interpretations are hinged on the signaling and bankruptcy cost theory.

1.4 Financial Performance of Commercial Banks

It is better defined as a level of business performance measured in monetary terms at a specified period of time say half yearly or yearly. Assessing the profitability performance an organisation offers chances to investor to evaluate the peril or advantages to them by connecting with that trade. Term stakeholders involve clients (borrowers), depositors (creditors), bank administration, the central government etc. These have variant interest in the performance of the banks. For instance depositors of the bank are interest in knowing that their deposits are accessible at any time they wish to make a withdrawal and there are no chances that the bank may go broke or insolvent and shut down with their hard earned cash. So this is why assessment of the performance of an organisation is critical so as to offer confidence to investors. Too evaluating the performance of an organisation helps management to assess the suitability of their strategic plans and alter or improve them accordingly.

Below discussed ways are the most common used to assess profitability and banks like any other organisation are of no difference since they utilise the same profitability measures. Financial performance is a monetary system to try and figure out to what extend is the organisation utilizing the available resources, or in other words to what extend is the organisation converting resources into profit. Mostly utilized measures of bank profitability are ROE, ROA, ROD, PER, NIM and cost to income ratio. Cost to Income ratio being newly evolving way of assessing business profitability. Be sufficient to say this study will make use of the two most commonly used that is ROA and ROE ratios in a trying to assess the profitability performance of the 10 banks under study.

Profitability assessors listed above can also be known as profitability ratios. Such ratios are fundamentally utilized as bank monetary ratios in trying to evaluate how a bank is doing profitability wise. When a ratio is comparatively high be it than the industrial sector average level or to its previously period ratio, or higher that is competitors level the banks financial performance is considered improving. Furthermost scholars in financial institutions writings used numerous financial performance proportion, despite that the following are topmost financial institutions performance benchmark, Iqbal et al (2005). ROE depicts the profitability to investors of the organisation after all costs and taxes deducted According to Van Horne (2005). Furthermore ROE is known to be a monetary proportion shows the assessor of net wage payback compared to investor's capital. Samad and Hassan (2000) attest that ROE is the return to investors to the devoted capital.

Typically organisations which access their finances through equity finances have higher ROE. Meaning the higher the ROE, the improved the organisation. According to Khrawish (2011) to ROE is the percentage of net pay subsequently to taxes expressed by Shareholder Equity. Ross (1994) also pointed out that the ratio is an administration competence measure. Put plainly ROE divulge how successfully a bank administration is exploits investors assets. Therefore suffice to allude, an enhanced ROE results in a further fruitful administration in terms of utilizing the investors' funds. Yet a higher ratio could be resultant of an improved ROA or monetary leveraging. A vital difference is drawn amid ROA and ROE by financial leverage in that financial leverage always enhances ROE. According to Ross et al, (2005) this situation is only permissible when aggregate ROA is greater than interest rate on borrowings.

The second ratio we going to look at which also works in measuring the monetary performance of financial institutions is ROA. Seen as a proportion that displays in what way worthwhile a financial house is proportional to the aggregate resources of the bank, Khrawish (2011). It is a ratio that shows profitability on aggregate assets of the firm consequently toward subtraction of entirely expenses, inclusive of the duty fares Van Horne (2005). ROA depicts a picture as to in what way management is on employing the available resources create revenue. Defined as an over-all benchmark of administration competence Westerfield et al (2005). Furthermore the proportion presents expertise of management creating earnings utilizing the assets provided (Khrawish 2011). That is the ratio expresses to what extend the firms is gaining per piece of a specified asset, moreover how banks might convert its assets into earning and gains (Samad and Hassan 2000). Wen, (2010) says that the larger the ratio the extra competent the organisation is in using assets. ROA depicts the proficiency of financial firm management to create revenue utilizing resources of the bank, although it may be bigoted due to off-balance sheet transactions, Athanasoglou et al (2008). Similarly firms could improve ROA by two methods i.e. either by enhancing profit margins or asset turnover nevertheless the two are impossible to be carried out at the same time as a result of competition and trade-off between margin and turnover.'

Vast hypothetical standpoint exist, that evaluates the relationships amid banking performance and capital structure. Even though the subsequent ratio will be left out are as assessors of financial performance in this study are generally employed in literature as profitability measures. NIM computes the difference between the interest earnings generated and the worth of interest paid, proportional to the amount of interest assets. Computed as below:

$$\text{NIM} = \frac{\text{Revenue interest from loans} - \text{Interest on Debt}}{\text{Normal Earnings Assets}}$$

The ratio can also be defined as disposable interest earnings expressed by aggregate earnings resources Gul et al (2011). Shown with this proportion are the expenses of bank intermediating duties and productiveness of the financial institute. The profitability of banks and net interest margin positively correlated implying the bigger the ratio the more efficient the performance of the banks.

ROD is amid top most quantifier of financial performance basing on a number of bank profitability academics. The ratio depicts proficiency of bank administration in employing deposits to generate revenues for the firm mostly through maturity transformation. Computed as:

$$\text{ROD} = \text{Profit} / \text{Aggregate Deposits}$$

Furthermore PER is also a determining factor of the financial performance of financial institutes. Measured here is functioning monetary performance of the organisation, looking at operation expenses specifically. Operating costs are revenue before levies and functioning costs. The aim of the proportion is to reveal the totality of operating earnings acquired for each dollar of operative expenses. This as well reveal competency of administration in controlling operative expenditures. The bigger the proportion the more expenditure proficient the bank is hence increased profitability Samad and Hassan (2000). Computed as follows,

$$\text{PER} = \text{Profit prior tax} / \text{Operational expenses}$$

1.5 Theories of Capital Structure

Organisations can gather finances through borrowing or issuing of shares (Ross, 2003). When it raise finance via borrowing, the organisation ought to return the money over an agreed period of time plus the cost of borrowing that is the principal plus interest. When the cash is raise via share issue no interest is paid but the stockholder will hold stake in the firm hence obtain a fraction of future earnings and cash flows of the firm through dividends? Shareholder are the owners of the organisation and what they contribute to the firm is called equity. Whereas contribution from borrowing through lenders is called debt financing. A choice in this case has to be done on how the organisation will be financed and the choice is known as capital structure decision. It is worth to mention that amongst decision in firm this one is a very critical decision. Capital points to the organisations source of long term funding.

Firms gather equity funding in two ways. To start with, they can sale fresh stocks. The investors who acquire the issued stocks offer cash in interchange of a portion of the firm's yet to come cash flow and earnings. Secondly, the firm can reinvest its extra profits into the business as a proxy for current stockholders. No share issue is done. What transpires if the firm does not put everything of the resources created by its current assets? The answer is so simple cash reserves are created which are utilized in the future, or the cash will be used to payout dividends to owners of capital.

Business is intrinsically risky. The finance guys ought to recognize the risks and be certain the risky are properly hedged or controlled. Brealey et al, 2011 alluded that debt finance has its own merits but too much of debt can render the organization bankrupt. Funding measures regulate in what way the worth of the organization is apportioned. The organization might govern its capital structure. Meaning, the organization may primarily have gathered the financial resources to capitalize on assets base by borrowing more as compared to being funded internally; hence it might ponder altering such combination through dispensing higher ordinary shares and utilizing the revenues to redeem part of its owing's. Funding choices such as these this can be made autonomously of the initial investment decisions. (Ross, 2003) postulated the decisions to issue debt and equity impacts the way the business is earnings are proportioned.

A couple of theories have been progressive in amplification the capital structure and profitability value of organizations. Below discussed are such theories;

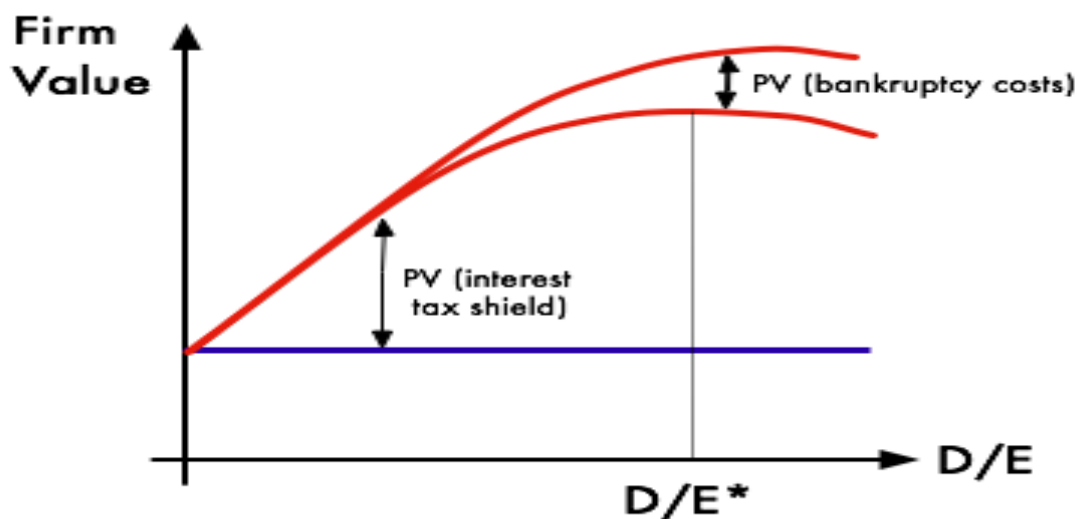
1.5.1 The Trade of theory

This theory hypothesizes that supervisors endeavour to adjust the advantages of interest tax shields contrary to the current estimation of the conceivable expenses of money related challenges (Myers 2001: 88). This hypothesis started from the investigation of Kraus and Litzenberger (1973: 911), who formally presented the premium duty shields related with obligation and the expenses of money related trouble into a state inclination demonstrate. As indicated by Chakraborty (2010: 296), the trade-off theory proposes that some type of ideal capital structure should exist according to the harmony between the present estimation of premium duty shields and the cost of bankruptcy. Bankruptcy expenses can be arranged under direct and indirect expenses. As appeared in Baxter (1967: 395), coordinate expenses of liquidation incorporate, inter alia, the regulatory and legitimate costs brought about by

a firm that goes bankrupt. Then again, the circuitous costs identify with the lessening in the market estimation of the firm due to the firms failure to benefit its obligation commitments.

As indicated by Barclay and Smith (1999: 10) the indirect expenses of bankruptcy can constitute a considerable segment of the market estimation of the firm. Having said this, the situation in capital structure hypothesis has been to decide to what degree obligation can be utilized with a specific end goal to counterbalance assess suggestions to the degree that the danger of exorbitant obligation is stayed away from. Figure 2.1 represents trade-off which transpires amid the current estimation of the assessment appropriation related with an expansion in use and the present estimation of insolvency expenses. This necessitates a scenario where organisations strive to acquire an ideal capital structure. At this stage the tax cuts are boosted whereas limiting the danger of liquidation, which emerges from the utilization of unreasonable obligation.

Figure 2.1: Trade off Hypothesis of Capital Structure



Adapted from: Brealey et al (2007)

They are 4 essential forecasts of the hypothesis which exist. Initially, the model forecasts that organizations have to have an objective obligation proportion and that these proportions will vary from organization to organization. This expectation is affirmed by Graham et al (2001) who voiced that most of the reviewed Chief Financial

Officers concurred that they take after an objective obligation proportion. Besides, the theory expects that organizations with generally benign unmistakable resources might be not as much be presented to the expenses of monetary trouble, and will in this manner, be required to obtain more. Then again, organisations with unsafe elusive resources will be extra presented to the expenses of budgetary misery, and will be relied upon to get less. This expectation is affirmed by Rajan et al (1995) representing organisations in seven created nations, Frank (2009) for non-money related organisations in the US and Qiu (2010) for non-monetary firms on the Australian Securities Exchange.

Thirdly, the theory forecast that greater minimal duty fees be related with more elevated levels of borrowings. This is a result of interest being duty deductible. Utilizing tests in view of incremental choices, MacKie (1990) archives that organizations encountered with advanced marginal taxes rates will probably have higher liability proportions, and organizations with less marginal tax fees will issue greater equity contrasted with liabilities. Utilizing information for in excess of 10 000 organization, Graham (1996) discoveries a factually noteworthy favorable relationship amid marginal tax rates and debt ratios.

Fourthly, according to DeAngelo, (1980), the trade-off theory forecasts that organizations with supplementary taxable income and comparatively few non-debt tax shields the likes of investment tax credits and depreciation will have additional inducements to borrow. In a bid to benefit from the interest tax shields, organizations with lesser non-debt tax shields must be projected to borrow more. Contrariwise, organizations with much non-debt tax shields must have reduced debt in their capital structure.

Bradley et al (1984) obtained antagonistic suggestion to this forecast. Report was a favorable link amid non-debt tax shields and firm debt to value ratios. These findings were also attested by Chakraborty (2010) form Indian organizations. This promising relation could as well be telling that organizations using extraordinary no borrowing levy shields the likes of amortization, own physical assets. Which allows sustainability additional dues. Contrary to that notion, Titman et al (1988) proved irrelevant adverse relation amidst leverage and no debt tax shields. As such, Ozkan (2001) utilized a vibrant capital structure prototypical for organizations firms in the Great Britain and attest a substantial adverse relation amongst leverage and non-dues tax shields.

Conclusively, considerable proof is present in lieu of the principal 3 core estimates of the trade-off principle. The fourth part forecast is judiciously reinforced. Utmost researches illustration that companies with additional non-debt tax shields carry supplementary obligation in their capital mix.

1.5.2 The Agency Hypothesis

The model is hinged on a viewpoint that administrators will not at all times behave in a way that benefits the investors particularly the ordinary shareholders. Jensen et al (1976) supplementary clarify this model through pinpointing binary major misunderstanding amid groups to an organisation, to begin with, amid the management and the owners, and then, amongst the owners or stockholders including the creditors. In initial scenario, management is attracted to keep the companies resources to themselves disadvantaging the owners of equity. The occasion that follows, liabilities allows investors motivate to finance sub-optimally. Basically when a security produces earnings greater compared the nominal value of the liability, the gains are enjoyed by the stockholders (Harris and Raviv (1991)). Equally, if the investment could not meet the expectation, the owners of equity are protected by the limited liability status of the company and go free. Left will be administrators with dues controlling an organisation whose prevailing market value is lower than the nominal value of the amount due.

Extra possible agency expenses of dues is propounded by Myers (1977). He takes note that when organizations are at virtue of collapsing, no impetus for investors to contribute personal funding is present, regardless of whether optimistic net present value ventures remain accessible. Such being on account that benefits obtained from the projects will enjoyed mostly by the debt holders. The suggestion is that high liability levels may bring about the dismissal of significant worth expanding ventures. Stulz (1990) contends that obligation installments may influence investors both decidedly and contrarily. On the positive note, debt payments drive supervisors to pay out premium in this manner lessening the potential over investment issue. On the negative side, inordinate obligation may prompt high premium reimbursements, which may prompt the dismissal of gainful tasks, accordingly prompting the under investment issue. Capital structure is in this manner controlled by a trade-off between the advantages and expenses of the debt.

Extensive work has been done to test the legitimacy of the agency cost theory. For instance, Kim and Sorensen (1986) recognize the nearness of organization costs in Compustat listed organizations as a solid connection between insider proprietorship and leverage. Vilasuso and Minkler (2001) utilize a dynamic model of capital structure on an arrangement of 28 freely held firms, and exhibit that agency costs are related with shifts in leverage. Harvey, Lins and Roper (2004) explore whether obligation can control the impacts of agency costs for an arrangement of developing business sector firms, and their agency costs. Evolved was a profit competent pointer as a determinant of organizations profitability functionality, and endorsed the forecasts of the agency philosophy which is greater leverage is absolutely connected to turnover competence, Berger et al (2006). Nonetheless, Brounen, et al (2006) review administrators in EU states and obtained they no signs worth recommending that agency costs impact capital structure choices. Generally, findings proposes that reinforcement of the agency principle exist.

1.5.3 Information Cost Theories

The theory is centred on data discrepancies amid commercial administrators and stockholders. Such statistics difference is better called information disproportionate. The resultant theories addressing these information difference are the signalling and pecking order hypothesis.

1.5.3.1 The signalling theory

The model exudes from data irregularities amongst organisations administration and investors. On the off chance that supervisors trust that their organizations are underestimated, issues liabilities initially then equity lastly if all else fails. However, if administration trusts organisations are exaggerated, equity is issued initially. The hypothesis was propounded by Ross (1977) alluding that is administrators have access to in house information, the capital structure decision they make will make available data to the market. Also affected by the hypothetical preface that increments

paying off debtors are a constructive symbol that administrators are certain of the future profit is leverage. Obligation indentures be dedication by supervisors to provide forthcoming interest instalments. Inability to reimburse owing's could prompt liquidation. Such signals certainty to the market that organisations might have adequate money streams to benefit obligation.

Investors to an organisation are lingering inquirers to organizations money streams. This is on the grounds that guaranteed interest instalments are a commitment and have need above dividends. Resultantly, securities costs are very delicate to money related organization declarations compared to security costs. On the off chance that supervisors are idealistic about their organizations forthcoming projections, organizations securities cost seems extra underestimated compared to bond costs. The model was analysed and proved a normal decrease of 3% on offer cost of an organisation which reported fresh value issues. Differentially, an insignificant decrease on offer costs succeeding obligation offering declarations exist. Likewise, increments on dues are related to expansion in stocks value yields approximately of 14% for obligation value replacements.

Organizations whose profit expanded next period are defined as underestimated corporations, and such organizations whose income diminished next period as exaggerated companies Barclay, et al (1995). Little measurably noteworthy positive relationship amongst leverage and unforeseen profit was attested. The ramifications of the signaling concept is that commercial director's endeavours to spot value offerings in view of markets appraisal of their offers. A solid connection amid an organisation funding selections and authentic market estimations of value is present Baker and Wurgler (2002). Generally, capital structure for a business is combined after effect of administration previous endeavours to spot the market. Be that as it may, Brounen et al. (2006) don't discover any confirmation to propose that European directors flag their private data to impact capital structure. The proof gave up to this point proposes that, all things considered, the signaling model applies.

1.5.3.2 The pecking order theory

The hypothesis makes signaling notion a single stride facilitate through proposing that data expenses are sufficiently significant to authorize administration to offer stocks managers with slightest data expenses (Barclay, 1999). Myers and Majluf (1985) initiated the model through showing that an offer is for the most part seen adversely by the speculators. This is on account of administrators trying to offer stocks during them being overrated. Expressed straightforwardly, the hypothesis recommends keeping on mind the end goal to maintain a strategic distance from the data impacts of new offer issues, a firm will probably offer liability than ordinary capital. This expectation is contingent on the manager's conviction that their organizations securities are under-priced.

The model infers management takes the easy way out, and that they will work down a pecking request by picking to issue the least expensive type of financing. For this situation, firms will decide on held income as it has no unfavourable choice issues. At the point when held income are depleted, the firm would then be able to issue debt. When it doesn't bode well to issue more liability, equity can be issued as a financing wellspring of final resort.

The pecking order theory proposes that organizations with few venture openings and high free money streams will have low debt proportions. Alternately, high development firms with low free money streams will have high liability proportions. Various investigations have affirmed the presence of the pecking order hypothesis. Rajan and Zingales (1995) use an informational index from seven industrialized nations, and they discover some proof for the pecking order hypothesis as a negative relationship amongst leverage and benefit. Utilizing an example of one hundred and fifty-seven companies in the US, Shyam and Myers (1999) discover bolster for expectations of the hypothesis. In spite of the fact that this is a compelling outcome, an example of 157 firms is generally little contrasted with totally the recorded organisations in the US.

As indicated by Frank and Goyal (2003), such brings up issues in the matter of whether the hypothesis is extensively relevant. Utilizing capitals flow information for more extensive cross-segment for US companies discovered was disposable equity offers track the funding deficiency further nearly compared to disposable dues offers. Such

discovering permits differentiating confirmation to forecasts of hypothesis. Helwége and Liàng (1996) give an immediate trial for model through looking at the capital structures of five hundred upcoming companies which opened up to the world in 1983. Discovered was utilization of outer funding is not part of the notion.

Despite what might be expected, Flannery and Rangan (2006) receive a fractional change model of firm use for firms recorded on the Compustat (CRSP) database, and they affirm the presence of a pecking order. Leary and Roberts (2010) use recreation methods to test the exactness of the pecking order hypothesis. They play out their investigation by permitting firm obligation ability to differ with substitute factors related with the trade-off theory. They find that the prescient energy of the pecking order hypothesis increments essentially with the variety. This finding proposes that the pecking order and the trade-off hypotheses assume a vital part in clarifying financing choices.

dSeifért and Gonénc (2010) relapse disposable obligation offers on budgetary shortage factors for organisations in 23 developing countries. The presumption was the pecking request funding is predominant particularly in such developing economies since offers of deviated data and noteworthy organization expenses. These financing loans back the hypothesis that funding choices are components of overall economic situations companies are operating within. Also, Bessler and Drobézt (2011) analysed impacts of lopsided data on organisations funding choices, and presumed that data irregularity are essential determinants of vibrant pecking request conduct. In particular, the likelihood of issuing value is reported to be more articulated with diminished data irregularities. From the actualities examined, it creates the impression that the confirmation on the pecking request hypothesis is blended, primarily on account of the strategy utilized and that financing choices are liable to various variables that may impact capital structure in an unexpected way.

1.5.4 Contracting Cost Theories

The hypothesis depend on under investment issue proposed by Myers (1977). The under investment issue can be represented as below; exceedingly levered

organization will probably leave behind venture openings due to the danger of non-payment. The issue is additionally aggravated with by the greater expenses of value related through companies with possibility of defaulting. It might make monetarily bothered organizations do without either resources or stock prospects. Expectations of the theory is that organizations with value which is inclusive principally of the current worth of immaterial securities prospects selects lower liability ratio. Such moderate way to deal with obligation offering is used so as to limit unfriendly impacts of the lower investment issue. On the other hand, huge develop firms with less venture open doors will pick high liability proportions on account of the lower plausibility of monetary trouble costs. This forecast is in opposition to the pecking order hypothesis which places that high development firms with moderately less money streams will have higher liability ratio.

Couple of researches have tried the theory through employing instability of revenue, expansion in assets, advancement in sales and the market to book ratio as a representative for expansion prospects. According to Bradléy *et al.* (1984) who utilized standard deviation of EBITD expressed over normal book assets as a representation for expansion prospects. The results show statistically substantial adverse association amid leverage and volatility. The connection is pragmatic to either un-regulated organizations or the entire organizations in sample. Barclay and Smith (1996) employed the market to book equity proportion as measure for expansion prospects, and attested an adverse and mathematically momentous affiliation amid expansion prospects and leverage. Mutenheri and Green (2003) employed the % change in total assets as a representative of development of a proxy of Zimbabwean listed companies, and what confirmed was a substantial and favourable association for after reform time.

Utilized was increase in trades as a representative of expansion prospects for organizations in Ghana, then confirmed an optimistic and momentous connection amid firm growth prospects and leverage (Abor and Biekpe, 2005). This affirmative relationship infers that growth organizations request supplementary money to fund investor prospects. Adam and Goyal (2008) establish that market to book assets ratio carries largest data with relation to investor prospects. Therefore, Frank and Goyal (2009) utilized the representation to appraise the present connection with leverage. They report a negative and statistically significant association amongst the market to

book assets ratio and three of the four measures of leverage. Ovtchinnikov (2010) employs difference-in-differences examinations to approximate changing aspects of capital structure of an organisation in liberalized sectors, and discoveries that companies expansion prospects are connected to lesser credit proportion.

Former suggestion proposes that when the proportion is utilized as substitution for investment prospects, an adverse association is typically recognized. Nevertheless, if expansion in sales and assets is utilized, an affirmative relationship is ordinarily sensed. The insight is simple; growth in an organizations asset base affords investors kind of collateral for loan issues. Conversely, the market to book ratio might contain a bigger ratio of intangible non-physical assets prospects. Accordingly, these companies select lesser liability.

1.6 Empirical Literature Review

In the course of recent decades' corporate fund analysts have dedicated impressive endeavours to change logic of capital structure into observation. The issue of building up an indisputable hypothesis of capital structure and planning observational exams such are sufficiently capable to give a premise to picking among the different speculations is as yet uncertain. The writings on connection amid organisational profitability and capital structure delivered blended outcomes (Taani, 2013). Consequently, connections amongst capital structure and organisations esteem have stood as the topic of extensive open deliberation. Aside from the original work of Modigliani and Miller (1958) accentuating on the insignificance hypothesis of capital structure and their ensuing modification considering the tax reduction of obligation financing Modigliani and Miller (1963), and in addition succeeding contentions and inquires about, for example, Static Trade-off Model of Myers (1984) including the pecking request hypothesis propounded by Myers and Majluf (1984) that contends opposite of static exchange off hypothesis, exact examinations exists which accentuates on connections amongst capital structure and profitability of companies.

Salim and Yadav (2012) performed an analysis utilizing panel methodology for an example of two hundred and thirty seven Malaysian recorded organizations on their

local securities exchange. Such investigation utilized 4 execution determinants ROE, ROA, Tobin's Q and EPS as dependent factors. With 5 explanatory variables LTD, STD, TD proportions and developments. Information is isolated into 6 parts that is building, customer merchandise, manufacturing merchandise, estate, property, exchange and service. Empirical results show that capital structure adversely affects profitability. The exact tests demonstrate that capital structure (particularly TD and STD) adversely impacts performance estimated by ROE. Then again LTD and TD carry adverse critical effect on company's profitability. Moreover, discoveries of the investigation propose an essentially constructive connection amid organisation profitability and capital structure. At long last outcomes demonstrate that Tobin Q carry an optimistic and substantial association with size for entire areas being investigated aside from property division with an adverse impact.

Shubita et al (2012) lengthen Abor's (2005), and Gill (2011) results concerning impacts of CS on performance through scrutinizing impacts of CS on financial performance of manufacturing firms trading on Amman Securities Exchange during 2004-2009. The study comprises of thirty nine firms, employed correlations and regression analysis. The findings exposed considerably adverse relationship among debt and financial performance. The results indicate that an upsurge in debt position is related with a reduction in profitability; thus, the higher the debt, the reduced the profitability of the organization. The findings as well depict that profitability raise together size and sales growth. The results of the study dispute preceding experimental readings such as Abor (2005). Yet comments centred on conclusions are presented to expand particular variables such as the organisation should ponder employing optimal CS and forthcoming study must explore simplifications of the results outside the industrial segments.

Shubita and Alsawalhah (2012) analysed CS and firm performance of the Nigeria trading companies basing on the Agency Cost Philosophy viewpoint using a proxy of 70 organisations. Panel data for the organisation were produced and evaluated. Double explanatory factors assisted as determinant of CS were employed: DR and EQT whereas financial performance as the dependent factor. The findings depict that DR is adversely connected with PROF, while EQT is positively related with PROF.

Mohammadzadéha et al. (2013) studied the link amid the CS and financial performance of pharmacological firms in Iran. Leading thirty firms were utilized as research samples for the period of 10 years. Net profit margin including debts to asset ratio were utilized as determinants of the dependent and independent factors in question, correspondingly and sales development was utilized as regulator factor. Findings indicated a momentous adverse association amid financial performance and CS structure which implies that pharmacological firms proved a Pecking Order Concept and the inside funding resulted in extra revenues.

Beside from non-financial organisations, some experimental research in financial segments exists. Taani (2013) inspected effects of CS on Jordanian banks performance. Yearly accounting records of twelve trading commercial banks were utilized for the period from 2007-2011. Multiple regressions was employed on profitability determinants the likes of NP, ROCE, ROE.

ROE, NIM, TDTF, TDTE as capital structure factors. Findings depict that bank performance, determined by NP, ROCE and NIM was to be expressively and absolutely linked with total debt; whereas total debt is established to be trivial in being influential to ROE in financial industry of Jordan.

The capital structure factors, total liabilities of the listed banks also documented statistics undoubtedly representative that, the total liabilities of the listed banks do not make a substantial influence on their return on equity. To the extent the size of the banks is concerned, the investigation uncovers that the size of the banks does not significantly affect their return on equity. However there was a kind of positive connection between the two factors amid the investigation time frame. In the meantime, the outcomes for returns on value and their times of task had a fundamentally negative connection between them, which means as the banks develop in age, their profitability levels decreases altogether. The connection between Capital Structure and Profitability, and also the effect of Capital Structure on Profitability over the banks by returns on equity, uncovers that the profitability of banks listed on the Ghana Stock Exchange diminishes essentially with increment in their aggregate leverage. Along these lines there is a reasonable sign that, Capital Structure significantly affects the profitability of the listed firms on the Ghana Stock Exchange. Likewise at an average total leverage ratio of about 76%, there exist a negative

connection amongst profitability and capital structure in this manner demonstrating that, the ideal capital structure for the segment is certainly not at least 76%.

Furthermore Goyal (2013) examined effects of CS on financial performance of community segment financial institutes in India trading on state securities exchange through 2008 to 2012. Panelised data and multiple regression methods was utilized to obtain the link amid CS features and financial institutes profitability. Results of research authenticated a robust optimistic dependency of short term debt to capital on the entire performance determinants. While, long term debt to capital having an adverse link with the dependent variables. The organizations size knowledge an optimistic link with factors (ROA, and EPS) and adverse with ROE. Assets growth suggested a progressive association with ROA, ROE and EPS.

Also, Yegon, Cheruiyot, & Sang (2014) practically examines the connection amid CS and the organization's financial performance of financial companies sector in Kenya, through employing panelised data obtained from the financial records of the firms listed on the Nairobi Securities Exchange from year 2004-2012. Linear regression model was utilized to explore the kind of link among CS and financial performance. The writer's justification behind the manufacturing particular examination is the idea that external factors seem to vigour organizations in the same sector in a like manner, hence causing the being of a sector particular CS. Result wise its recorded that short term debt have substantial optimistic link with profitability. Such recommends that short-term debt inclines to be a little costly, and consequently extra short-term debt in CS lead to an increase in profit levels. As a result short term debt is the desirable source of funding for better financial performing organisations. While long term debt has substantial adverse association with the profitability that predict long-term debts are comparatively more expensive due to some direct and indirect costs, hence using high ratios of long term debt in financial structure results in poor financial performance.

Observational outcomes show no noteworthy relationship between total debt and profitability the slant of individual outcomes give the legitimate support to amazing outcome. Based on these discoveries it is inferred that the connection between short term obligation and the profitability is predictable with the static exchange off hypothesis not due to the tax shield rather some other unexplored factor. The basic soundness is, enthusiasm on long term obligation is likewise impose deductible cost

like short term obligation yet the outcomes are very inverse in course. Pecking request hypothesis is valid however with the expansion of short term debt over the chain of importance of inclination. Understood in such testing is that the two speculations have certain components that are fundamentally unrelated. Both the hypotheses all in all can remain constant however with the proposed backups.

As for the Ethiopian case, no empirical research straight connected with the subject matter understudy, "The effect of CS on effectiveness of Commercial Banks of Ethiopia" with a stress on essential commercial processes financial performance of banks. Nevertheless, there are a few researches in particular spaces of commercial business. Usman (2013) studied the determining factors of CS of large taxpayer stock firms in Ethiopia. Statistical examination were employed for a panel of thirty seven trading firms in Ethiopian Revenue and Customs Authority (ERCA) large taxpayers' branch office in Addis Ababa for the research era 2006 to 2010. 9 conventional independent factors were embraced in the research, including financial profitability, size, age, tangibility, solvency, non-debt tax shield, growth, and dividend pay-out ratio and earnings volatility.

Due to the enhancement in the current approximation approaches which permits to employ cross-sectional and time-series data simultaneously, random-effect panelised data regression was employed to research the impact of designated explanatory factors on CS. Findings indicated that size, age, perceptibility, solvency position and non-debt tax shield of a firm were favourably connected with leverage, while financial performance, incomes instability and disbursement pay-out proportion are adversely linked to leverage. Development factors were observed as immaterial on impacting leverage of large taxpayer stocks firms in Ethiopia. Centred on signals of such links the writer showed that, Agency cost philosophy offer extra substantial signal as compared to another CS models in clarifying CS of large taxpayer share firms in Ethiopia.

Additionally, from pragmatic researches in banking segments of Ethiopia Wildemikael (2012) scrutinized association amid leverage and organization precise causes of CS choice, and the concepts of CS that can clarify the CS of banks in Ethiopia utilizing a varied method study method by conjoining documented investigation and in-depth conferences. Additional precisely, the research utilized 12 periods (2000 - 2011)

statistics for eight banks in Ethiopia. Results show that productivity, size, tangibility and solvency of banks are substantial essentials of CS of banks in Ethiopia. Conversely, development and risk of banks are seen to have no statistically substantial effect on CS of banks in Ethiopia. To add on to that, hinging on findings of examination the writer showed that pecking order philosophy is relevant philosophy in Ethiopian banking sector, while less suggestion to sustenance static trade-off philosophy and the agency cost theory. Henceforth, the writer suggested banks to give due concern to viability, size, solvency and tangibility in their grit of best CS.

2. CHAPTER: RESEARCH METHODOLOGY

2.1 Introduction

Methodology is well-defined as the investigation and rationale of employing a certain method for a specific research, it can also be demarcated as systematic and methodical approach used to collect data from which information is attained. Thus the procedure that was used in this schoolwork largely applied computable techniques by using an econometrics software, called E-Views (Student Version 7) to examination for the distributed-lag O.L.S regression, Panel data econometric model and lastly eloquent statistics. This chapter will reconnoitre the various techniques and methods that were used in analysing the connection between impacts of the capital structure on bank performance in Jordan.

2.2 Research Design

As already alluded to, the question of whether capital structure would have implications on bank performance is empirical interrogation which desires to implore geometric and mathematical practises to study their associations, thus both qualitative and reckonable techniques employed. Cooper and Schandler, (2003), maintain that the recognised study begins were the investigations leave off. The regression breakdown (ordinary least squares) and interconnection tests are the main riggings to be labouring to yield results that will be painstaking for policy endorsements. To add value to the study investigational design was also engaged were an econometric model was used to regulate the statistical connexion of variables that are being tested.

2.2.1 Panel Data Regression Models

These are prototypes that association time sequences and cross-sectional explanations, also called longitudinal data where numerous cases are observed and more stretch periods. Two types of evidence are found in cross-sectional interval series data – those replicated in the differences amongst focusses or exclusive subject information imitation in changes inside subjects over interval thus board data worsening procedures permit you to take advantage of these dissimilar types of

information. The benefit of using panel data is that it is possible to regulate for some types of misplaced variables even minus detecting them through perceiving fluctuations in the reliant on variable over time. This controls for mislaid variables that fluctuate between cases but are continual over interval. Square data can be used to control for absent variables that dissimilarity over time but are perpetual amongst cases.

A panel data set must have data on n circumstances, overt times segments for a complete of $n \times t$ explanations, this is in prolonged, (Torres- Reyna 2007). This data can also come in what is wide method with one observation per case and variables for each different value at each dissimilar time period. This can be seen in the panel regression model below. The data was first converted into long form before it was put in the model. The limitations of rectangle data include data assortment issues, specimen design, treatment which is non-response in case of micro panels or off-road reliance in the case of macro panes for sample where there is connexion amongst kingdoms.

2.3 Data sources & Collection methods

The data will be collected from the Amman Stock Exchange and will be yearly data from the period 1999 to 2016 giving a total of 108 observations. This study makes use of mainly secondary data which embraces statistics that have already collected for another agendas, perchance normally because of its and continuously safety of the data. Such information is assimilated in available achieves on the topic. Sample of the study is panelised data of 6 banks in Jordan for the period from 1999 to 2016. Financial institutions internal factors are together, obtainable and premeditated in the financial records for example the cash flow statements of the firms being studied. Financial accounts would be acquired on the online sites of the specific organisations, Federal Bank of Jordan as well as the sanctuaries and stock discussion of the this countries. Affecting macroeconomic determinants will be attained from World Bank, IMF and another journals. Ghauri and Gronhaug (2005), contends in sustenance of exploiting these arrangement of statistics, and determined numerous examination requirements

and targets crucial improvement of employing secondary statistics is the mammoth reduction of expenditure perceptibly time also funds.

2.3.1 Rationalisation of Data Collection Technique

Secondary data collection attitude is commonly less affluent and more reachable since the information is available from countless archives for example World Bank, libraries and statistical offices. The evidence and data attained through secondary is frequently convincing and authorized subsequently most of it is second-hand in publishing economic trends for the nation and other state reports. This makes the material more reliable and less prejudiced to personal conclusion.

2.4 Data Presentation & Analysis Techniques

Information attained in diverges foundations as declared in subgroup 3, 5, 1 was industriously and expressively analysed while the entire statistical procedures laboured to ensure that statistics will not produce bogus findings, basing on non-fiction the research exploited ROA and ROE as quantity of profitability and were degenerated in contradiction of such illustrative factors as size of the bank, CAR, CIR, LR, GDP growth and CPI and regression outcomes were gained. Conclusions were tabularised and exploited so as for drawing of assumptions and endorsements concerning the connection amongst bank routine and productivity elements in Jordan. Demonstration and exploration of data misusing the pertinent implements should be completed in the chapter.

2.5 Econometrics Technique

A plate Data econometric method was implemented for the study, the main aim of the square data breakdown technique is to do away with two major weakness of most rough data modelling. This involve giving banks under study an equal weighting

regardless of whether the banks has different capital structure or asset base or small thus assume homogeneity. The accumulating of statistics with the similar parameters over time and crosswise districts that could be common per greatest panel statistics models begins by presupposition of independence transversely calculations. To this end the econometric analysis in the paper applied the Panel Least Square regression. The argument or inferences thus far propose that multi-linear deterioration model illumination the connexion between capital structure and bank performance was employed. This model was used as it integrates the effect of bank profitability indicators which will be the autonomous variable in this case.

2.5.1 Model Specifications

PLS regression process will be exploited and regression prototypical run by the statistical package Econometric-views as an endeavour bargain connexion amid bank productivity and inside factors of productivity. Subsequently of the data being panelised, panelised statistics examination were employed. The panelised information could promote an extensive method to scrutinise several periods and the diverse banks since it calculates cross-sectional and period succession Figures confirmed for unit root, connection, also autocorrelation. Immobile Outcome model and Random Effects model to be put to the statistics and Hausman examination utilized for selection of the model which well pronounces the data. Subsequent demonstrations was calculated for the issue. The model assessment development will be done using a commonplace least squares regression attitude. The use of this attitude allows one to regulate the enormousness of consequence as well as the significance of the relationship between the variables (Granger & Newbold, 1974).

From the established research problem and empirical literature, it has been noted that changes in financial performance is determined by capital structure (CS) proxy by debt ratio (DR), Ratio of total liabilities to total assets (LAR), loan to deposit ratio (LD), firm size (SIZE) and the extent to which the assets are Ratio of equity to total assets (EAR). Return on assets (ROA) and return on equity (ROE) will be used to determine changes in financial performance (FP). 1But it has been established that the financial enactment of banks listed on the Amman Stock Exchange has been varying in

response to changes in DR, DER, LD, SIZE and TAN. Incorporating these into function (1) results in the formulation of the following function;

$$FP = F (DR, LAR, LD, SIZE, EAR) (1).$$

By introducing regression analysis in eqn.1 the following expressions are obtained;

$$\text{Model 1: } ROA = \alpha + \beta_1 DR + \beta_2 LAR + \beta_3 LD + \beta_4 SIZE + \beta_5 EAR + e_i (2).$$

$$\text{Model 1I: } ROE = \alpha + \beta_1 DR + \beta_2 LAR + \beta_3 LD + \beta_4 SIZE + \beta_5 EAR + e_i (3).$$

However, data conversion to logarithms will be done prior to estimation of the OLS. Such has been discovered by (Zarembka, 1990) to be helpful because it helps to deal with heteroscedasticity problems as well as having extreme parameters value. Thus the estimated model can now be expressed as follows;

$$\text{Model 1: } LROA = \alpha + \beta_1 LDR + \beta_2 LLAR + \beta_3 LLD + \beta_4 LSIZE + \beta_5 LEAR + e_i (4).$$

$$\text{Model 2: } LROE = \alpha + \beta_1 LDR + \beta_2 LLAR + \beta_3 LLD + \beta_4 LSIZE + \beta_5 LEAR + e_i (5).$$

Where:

ROA: Return on Assets for banking at time t

ROE: Return on Equity for banking at time t

DR: Debt ratio of banking at time t

LAR: Liquidity Adequacy Ratio of banking at time t

LD: Loan to Deposit Ratio of banking at time t

SIZE: Total Assets banking at time t

EAR: Equity to total Assets Ratio of banking at time t

Model one will degenerate the affiliation amongst bank effectiveness with ROA as a commission for bank profitability and interior factors effectiveness (explanatory variables). Second model regresses the relationship amongst marketable bank effectiveness using ROE as a representative for bank cost-effectiveness and internal elements of performance.

2.6 Variables of the Model

Financial ratios are useful indicators that reflect the financial performance of an organization and can be calculated from the financial statements. To test the impression of the capital structure on the financial routine of Jordanian companies registered on the Amman Stock Exchange, a multivariate analysis, based on three ratios, is used to measure the performance of companies. Characteristically in bank productivity nonfiction, 3 factors are exploited to determine banks' profits i.e., ROA, ROE, and NIM. This schoolwork employed ROA and ROE. Guru et al. (1999) harmonized with Rao and Lakew (2012) accentuate that proportions, unlike absolute figure of profits, are exploited in determination of bank efficiency since proportions are not artificial through unusualness in common price stage and are utmost frequently employed ratios in determining bank profitability in literature. Additionally based on previous works they also employed ROE and ROA as benchmark to determine bank productivity and as reliant on factors in similar snuffle.

2.6.1 Dependent Variables

2.6.1.1 Return on Equity

The ratio produce yield on stockholders' funds. Gained through articulating disposable profits over middling funds and articulated as proportion as below:

$$\text{ROE} = \text{Disposable Profit} / \text{Normal Stockholders' Equity}$$

Meanwhile ROE is as well normally employed in bank productivity writings, scholars has demonstrated that it is not the greatest apposite performance needles for financial institutions banks.

2.6.1.2 Return on Assets

Conferring to Davydénko, (2010) the proportion represents to what extend productive a financial firm controls its resources to create revenue. Kosmidou (2008), confirm that effectiveness of financial firms is furthestmost outstandingly shown through this proportion since it indicates the finest pointer of the competence of an institute to yield

incomes employing its accessible resources. ROA demonstrates the turnover enlarged on each resource unit and that is dominant, it describes the government's volume to utilize the bank's monetary possessions to generate paycheques and yields. According to Golin (2001), ROA has developed as the principal proportion for the control of the feasibility of banks, hence has achieved acceptance as the utmost employed proportion in bank profitability literature. Although it seems as the greatest proportion to determine effectiveness ROA is as well influenced owing to off-balance sheet events, Flemini et al., (2009). ROA is engaged as extra significant and more apposite productivity gauges and dependent factor. The percentage is calculated follows:

$$\text{ROA} = \text{Net Profit} / \text{Overall Assets}$$

2.6.2 Independent Variables

2.6.2.1 Debt Ratio

This represents the level of the banks' debt in relation to equity. The higher the level of the debt the more it will dilute shareholder interest and this is also considered to be costly as interest payments can be so high in most cases. Hence, a negative relationship can be foreseen (Sibilkov, 2009). This is one of the most frequently used needles for gauging the degree of use of peripheral financing foundations in the corporation's bankrolling structure and influential the quantity of debt per JD of total assets. This ratio is an gauge of the size of the company's probable debt burden. If this ratio is greater than 100%, this indicates that the company's debt is greater than its assets, meaning that the company will face the risk of being unable to meet its long term commitments, which expose him to the problems of bankruptcy and liquidation. If this ratio is low, it indicates that the company relies more on self-financing than on debt, and we can say that the bank has more assets than its debt. (Sheikh, 2008).

2.6.2.2 Liquidity Adequacy Requirements (LAR)

Opinions to the capability of the bank to concealment its arrears as they become due, henceforth this proportion expresses to a bank competence to own satisfactory liquid assets. Proportion of liquid assets/total assets is exploited as depiction of creditworthiness. Complex proportions depict that the bank is extra solvent. The meagreness of fluidity is among the vital errands for the disappointment of banks. However, liquid assets carry a lower return which substantial impacts efficiency. A favourable noteworthy connection was gained through Bourker (1989) amongst solvency and productivity. Even so, throughout times of haziness banks valour favour to progress their liquid property to assure in contradiction of risks. Numerous researchers saw an adverse connection amid solvency and banking proceeds.

2.6.2.3 Loan to Deposit Ratio (LD)

This provides a quantity of liquidity and the more a bank is liquid, the more it will be able to meet short term obligations and invest in profitable projects and assets which leads to an increase in profitability. Hence we can anticipate a positive relationship (Naimi, 2008) Factors manipulating bank's benefit is its helpfulness as appraised by the loan to deposit ratio. The cost to income percentage, categorised through expenditures articulated as operative incomes, can be consumed for benchmarking through the bank while appraising its functioning efficiency. Hess and Francis (2004) observed an adverse link amongst loan to deposit ratio and the bank efficiency. Ghosh et al. (2003) similarly initiate standard damaging linking midst expertise and the CIR looks to exist. Nevertheless, loan to deposit ratio, with its limitations (Welch, 2006), is another emergent measure of bank's efficiency and a benchmarking metric (Hess and Francis, 2004)

2.6.2.4 Size Total Assets

Size will be measured using the amount of total assets which the banks are in possession of and such is assumed to be positively related with financial performance (Sheikh, 2008). Bank size is unrushed by a total number of Assets under the bank's balance sheet. Being one of illustrative factors bank sizes capacity leads to economies of scale which resultantly reduce nominal expenditure through dispersion FC to a broader scale of assets which in turn has a favourable

impact on bank earnings. Athanasoglou et al, (2005) allude that similar respire if size of the organisation becomes bigger, features of diseconomies of scale settles, since the organisation will be extra huge to manage as well bureaucracy becomes the order of the day hence reduction on. An unswerving favourable connection is predictable amongst bank size and viability (Gul et al, 2011).

2.6.2.4 Equity to total Assets Ratio (EAR)

A demonstrative of the bank equity, the ratio of equity to assets is labouring. Equity to asset ratio procedures how much of bank's assets are funded with owner's assets. This ratio refers to the percentage of shareholders' equity in financing the Bank's investment activities (assets) and indicates the percentage of ordinary shareholders in the event of liquidation (Sheikh, 2008). Bestowing to the literature evaluation, academic examination is mixed vis-à-vis the affiliation amid the capital ratio and bank's effectiveness. Agreeing to risk-return trade off, a higher proportion indicates a lesser expected yield. Contrasting to the risk-return proposition, Berger (1995b) scrutinized the signaling premise and bankruptcy cost suggestion; portentous that a higher equity to asset ratio rise effectiveness owing to lesser expenses of monetary anguish. Consequently, an abstruse connection among capital proportion and bank's efficiency lives. Conversely, the reading expects a constructive construction amongst EAR and bank production since enough-funded banks face a lower cost of being ruined thus reducing cost of subsidy and risks.

2.7 Justification of use of e-views (econometric model).

Econometric-view package was employed for PLS guesstimate degenerating ROA and ROE and factors for productivity fortitude. PLS do has a numeral of expectations for it to hold factual which include but not inadequate to multi-collinearity amid factors persistent discrepancy of error term, no serial association amid error term which indicates that the error term have 0 predictable worth. $E(U_1) = 0$. Econometric software was employed to analyse the data through the regression model and a model connecting bank effectiveness to interior and exterior elements of effectiveness was

considered. The issue of unit root is a substance to pay consideration if working with regression. Non stationary data carry dual challenges for conformist regression analysis. Regression of further than 2 unlike random walk elements together with every outcome in relationship coefficients that are minor associated to their equivalent standard error far lesser than as per the forecasts of the expectations of stationary regression. The happening challenge creates with truly linked non-stationary effects that are combined in directive one.

3. CHAPTER: DATA ANALYSIS AND PRESENTATION

3.1 Introduction

The major purpose of segment of the paper is to present finding obtained from the approximation of the regression equation and to as well interpret the finding acquired from regression. Furthermore in the empirical analysis part, the notion is to examination the regression classical. The examination made utilization of quantifiable investigation of the impression of capital game plan on productivity of banks In Jordan amid the dated 1999 to 2016. As expressed in section 3, investigative test: association trials, and prototypical guess will be open and cleared up in this part. Clarification of movement results is to track and a quick will finish the section.

3.2 Data Testing and Sorting

3.2.1 Unit Root Testing

To go around manufactured results, the instrument to do in a relapse show is checked if the information is stationary. The E-views programming is dynamic to assess if every one of the factors are stationary or then Panel unit root test to confound if the factors are stationary developing on Levin, Lin and Chu, Im, Pesaran and Shin W-detail, ADF-Fisher Chi-square and PP-Fisher Chi-square. Amiably these advancement us in critical which level of vital α (Alpha) 1%, 5%, 10% we can castoff the invalid theory (H0) which includes that the groupings isn't fixed and acknowledge the substitution speculation (H1) if the arrangement are stationary. As can be described from the beneath counter the majority of the model's factors are measurably irrelevant at level were made lasting at the first adjustment in insusceptibility of dejected factors.

Table 3.1 Unit Root

Variable	Levin, Lin & Chu t*	Im, Persaran & Shin W-state	ADF-Fisher Chi-Square	PP-Fisher Chi-square
DR*	0.4318	0.5758	0.4513	0.6172
	0.0000	0.0000	0.0002	0.0000
EAR*	0.4647	0.6896	0.6135	0.7618
	0.0000	0.0001	0.0003	0.0000
LAR*	0.0104	0.3926	0.4645	0.2247
	0.0000	0.0000	0.0000	0.0000
LD*	0.9990	0.8365	0.7870	0.0023
	0.6420	0.0011	0.0005	0.0000
SIZE*	0.0448	0.9343	0.9711	0.9909
	0.1823	0.0260	0.0447	0.0319
ROA	0.0003	0.0003	0.0009	0.0035
ROE	0.0283	0.0092	0.0009	0.0019

Source: Primary Data*stationary at 1st difference

3.2.2 Correlation Analysis

The examination is done to evaluate the strength of linear relationship in the midst of the components. That is in an exact model when at least two free factors are capably interconnected to each other a gravely acted of multi-collinearity will surface. Significantly, multi-collinearity hard to isolate the effect one logical flexible on the ward from the impressions of the other informative components. Anyway not autonomous elements are normally connected to each other, of fixings is the level of relationship. Anderson, et al. (2011) by using the manager of skim test say that any association coefficient outperform 0.70 or under - 0.70 demonstrates the approaching issue of multi-collinearity.

So also, multi-collinearity is a model odd tested as compared to the entire populace where the example was aggregate from, in this regard a substitute model may not

present the very degree of co-linearity among the autonomous variable. Multicollinearity is a straight relapse partnered issue that is clear in bothered parameters gauges and without question that makes it trying to analyze the impacts of the free factors on the reliant variable. For the assurance of this theory, a connection investigation was keep running as introduced in the beneath table 4.2.As what can be seen from the underneath table, multicollinearity was not an issue in this paper since all the relationship coefficient were not as much as the general guideline (0.70 and - 0.70).

Table 3.2 Correlation Matrix

	DRD1	EARD1	LARD1	LDD1	SIZED1
DRD1	1				
EARD1	-0.103689	1			
LARD1	0.088158	-0.069424	1		
LDD1	-0.019538	0.048823	-0.048730	1	
SIZED1	-0.109071	-0.173336	-0.064184	-0.004385	1

3.3 Diagnostic Test

Diagnostic tests were complete through testing if any serial correlation among variables exists, multicollinearity,co-integration and blimey of fit tests. Such quizzes are crucial to assess the excellence of the classical and adherence to the expectations of the Panel regression model and the numerous linear regression representations and to examination how well the model suits the data. These quizzes assess the model insufficiencies afore it may be employed to forecast forthcoming values, inevitably such finding to this schoolwork are below recorded.

3.3.1 Serial Correlation

Checking information have any serial connection which may prompt false outcomes, the Durban Watson was assessed and the Durban Watson should be over 1.50 yet underneath 2.3 for the information to be free from serial relationship. Since our prototypical outcomes had a Durban Watson estimation of 2.10 for ROA and 2.16 for ROE, it requires that they were no serial relationship.

3.3.2 Goodness of Fit Test

The portrayal's F measurement for both the generations is condition 1 for ROA and condition 2 for ROE were inspected. The F-measurement for display 1 was direct at 11.12 and the probability F-insights of relapse of 0.00000, which is less 5% critical level achieve that the model incredible. The F-measurements for show 2 is 27.48 is sensibly high plausibility F-insights of relapse of 0.00000 recommending model 2 is a solid match moreover. Rather specified to as the coefficient of various guts for various relapse or amount of backbone R2 is in a few occasions unceremoniously utilized as a blimey of fit measurements and used to hand-off the authenticity of compounding revelations under included depiction of informative varieties in the model. R2 is unequivocal as the extent of fluctuation in Y (the ward capricious) that is clarified by the lighting up flexible x variable.

the effects of the free factors on the needy variable which is ROA and ROE in this manner the effect of the capital structure on the budgetary execution banks in Jordan. Continuously the R2 for the primary model which connote the ROA is 0.75 which derives that 75% of the variety in ROA is clarified by the model or by the logical factors. Thus, the R2 for the second model which portray ROE is 0.63 which implies 63% of the varieties in the Y factor are clarified by the logical variable (Bank estimate, obligation to value proportion, credit to stores proportion, Liquidity Adequacy Requirements, and Equity to add up to resources proportion). Regardless, R2 have some confinement, in the first place the measurable discoveries base on the vital hypothesis that our model is right. Furthermore, R2 is excessively open, making it impossible to the quantity of the autonomous factors in the relapse display. Estimation an extra logical whimsical to the relapse demonstrate is more induced to advancement the R2 as differentiating to falling it. Along these lines on the off chance that one is

excited to have a higher estimation of the R2 can essentially add more factors to the model whether they are generous or not. Additionally, R2 does not speak to whether a relapse show is tasteful, which means one limit have a low R2 esteem for respectable model or a high R2 esteem for a model that do meet all requirements for the information.

To evacuate these inquiries of R-squared, acclimated R-squared is arranged, since balanced R-squared foresees the representation estimate. In our exploration, the balanced R-squared for demonstrate 1 is 0.69 that is subsequent to spellbinding into translation the degrees of self-assurance the model illuminates 69% of the dissimilarities. Display 2 the adjusted R-squared is 0.61, representation that after since the degrees of opportunity the model edifies 61% of the dissimilarities in ROE. Balanced R-squared holds an amount of characteristics which makes it a searched for integrity of fit amount related to R2. On the off chance that new factors are added to the relapse demonstrate R2 dependably increment, while the balanced R-squared can rise or fall restrictive on the outcome of the additional factor. That balanced R-squared is utilized to screen the variable to incorporate into the model since it just escalations when you include a critical factors and decline when you include a unimportant variable.

3.3.3 Co-integration

Pedroni Residual Co-integration test was carried out to verify if the variables are co-integrated in any way and the results as shown from the table below show that no co-integration exist since of the 7 methods used only 2 are statistically significant at 5% level.

Table 3.3 Pedroni Residual Co-integration test

	Statistics	Prob.	Weighted Statistics	Prob.
Panel v- Stats	1.710334	0.0436	-2.831051	0.9977
Panel rho Stats	1.270122	0.8980	2.376579	0.9913
Panel PP- Stats	3.002855	0.0013	7.729401	0.0000
Panel ADF- Stats	4.329462	1.0000	-0.223633	0.4115
Group rho Stats	3.277207	0.9995		
Group PP- Stats	-10.25821	0.0000		
Group ADF-Stats	0.734991	0.7688		

3.4 Model Selection

The two models expressed in part 3 that model 1 for ROA and model 2 for ROE under prototypical game plan were snug into the information. Both settled result prototypical and arbitrary result display were customized and a Hausman test was utilized to fantastic the original assigns the information. Table 3.4 and Table 3.5 beneath depict the results from the Hausman test for the two portrayals.

Table 3.4 Hausman Test: Model 1 ROA

Null: Random effect model good method

Alt: Fixed effects model is the best model

Test summary	Dependent variable	Chi-Sq df.	Prob.
Period random	ROA	46.656450	0.0000

Source Primary Data

Results demonstrate FE prototypical is tight to the information thusly the likelihood is 0.0000 which is subordinate than 0.05 the considerable close, consequently concede the other recommendation conditions that the relentless assets established is the best prototypical. Therefore, the steadfast belonging model is utilized to dissect the belonging of a lighting up flexible on ROA.

Table 3.5 Hausman Test: Model 2 ROE

Null: Random effect model is the best method

Alt: Fixed effects model is the best model

Test summary	Dependent variable	Chi-Sq d.f.	Prob.
Period random	ROE	3.485653	0.7459

Primary Data

Accordingly we concede the invalid theory since the prob. esteem is 0.7459 which is more than the 0.05 the earth shattering level. Thus the discoveries portrays that the RE prototypical is to be fitted to the information. Significantly, the irregular belonging model is to work to think about the belonging of the self-deciding variable on ROE.

3.5 Empirical Results from Regression Model:-

The Impression of Capital Structure on Financial Concert of Commercial Banks in Jordan.

3.5.1 Regression Results

Table 3.4 and 3.5 beneath portrays the estimated limitations and t-statistics gifted from the submission of random properties model for both ROA and ROE as reliant on variables.

Table 3.6 Relationship with Return on Assets

$$\text{ROA} = -0.000750 \cdot \text{DR} + 0.088871 \cdot \text{EAR} - 0.022257 \cdot \text{LAR} - 0.0000651 \cdot \text{LD} + 2.02 \cdot 10^{-15} \cdot \text{SIZE} + 0.003351$$

	Debt to Equity	Equity to Asset	Liquidity Adequacy	Loan to Deposit	Bank Size	Constant
Coefficient	-0.00075	0.08887**	-0.0225**	-0.00065	2.02E-15	0.003351
t-statistic	-0.08103	5.091631	-3.01893	0.495005	0.040139	2.943109
Prob.	0.9356	0.0000**	0.0034**	0.6220	0.9681	0.0043
R-Squared	0.755826	0.755826	0.755826	0.755826	0.755826	0.755826
R-adjusted	0.69	0.69	0.69	0.69	0.69	0.69
F-statistics	11.11542	11.11542	11.11542	11.11542	11.11542	11.11542
Prob.(F-statistics)	0.000000	0.000000	0.000000	0.000000	0.000000	0.000000
Durbin-Watson stat	2.109125	2.109125	2.109125	2.109125	2.109125	2.109125

i) Impact of Explanatory Variable on Return on Assets (ROA)

The Debt to Equity Ratio variable is undesirably related to Return on assets with a coefficient of (-0.000750). This means that a 1% intensification in Debt Equity ratio will reduce Return on Assets by 0.0008 units. The variable however is not statistically significant as the probability statistics value is 0.9356 which is above the required 0.05. This means that for banks in Jordan any increase in debt over equity would result in a decrease in the return attributable to shareholders. Banks in Jordan ought to therefore implement measures that reduce the debt levels to manageable levels and increase equity.

The Equity to Assets ratio variable is significant at 0.0000 which is less than 0.05. The coefficient is positive meaning there is a positive relationship between equity to assets and ROA among banks in Jordan. The coefficient value of 0.088871 indicate that a 1% increase in Equity to Asset Ratio would increase Return on Assets by 0.09 units. This shows that for banks in Jordan if shareholders focus on increasing the equity to assets ratio the banks would see their return on Asset ratio increasing.

The Liquidity Adequacy ratio is statistically significant at probability value 0.0034, the coefficient is negative related to Return on Assets with value (-0.022257). This means that any increase in Liquidity Adequacy by 1% would see Return on Assets falling by a small insignificant value of 0.022 units. The six banks under study would see their ROA slightly falling should they opt to increase their Liquidity adequacy ratio. The Loan to Deposit ratio (LD) is not statistically significant in the model at 0.6220 probability which is more than 0.05. The coefficient of (-0.0000651) signifies a negative relationship between Loan Deposit ratio and return on Assets. The banks in Jordan would see the return on assets falling if the loan Deposit ratio increases.

Bank size variable is statistically insignificant in the model with probability statistic of 0.9681, the coefficient is (2.02E-15). This shows that a positive relationship exists between bank size and return on assets for banks in Jordan, the more the bank increase in size, the more the return on assets ratio due to benefits of scale economies.

Table 3.7 Relationship with Return on Equity

$$\text{ROE} = 0.002713 \cdot \text{DR} + 0.086339 \cdot \text{EAR} - 0.020313 \cdot \text{LAR} - 0.00000251 \cdot \text{LD} + 0.019667 \cdot \text{SIZE} + 3.11 \cdot 10^{-13} + 0.003463$$

	Debt to Equity	Equity to Asset	Liquidity Adequacy	Loan to Deposit	Bank Size	Constant
Coefficient	0.002713	0.086339*	0.0203-**	0.00000251	3.11E-13	0.003463
t-statistic	0.299665	5.196196	-2.939590	-0.196545	0.402027	3.338717
Prob.	0.7651	0.0000**	0.0041**	0.8446	0.6886	0.0012
R-adjusted	0.61	0.61	0.61	0.61	0.61	0.61
R-Squared	0.634459	0.634459	0.634459	0.634459	0.634459	0.634459
F-statistics	27.48147	27.48147	27.48147	27.48147	27.48147	27.48147
Prob.(F-statistics)	0.000000	0.000000	0.000000	0.000000	0.000000	0.000000
Durbin-Watson stat	2.166629	2.166629	2.166629	2.166629	2.166629	2.166629

ii) Impact of Explanatory Variable on Return on Equity (ROE)

The regression equation table shows of the five variables one is adversely related to ROE The Debt ratio is statistically insignificant with probability value of 0.7651 and a coefficient value of (0.002713). This shows that for every 1% increase in Debt the return to shareholders or equity provider's increases by 0.003 units. Too much debt funding is detriment to the company of any institution. The results are not as per expectation. The focus by management should be to minimise debt funding and strike a stable balance between debt and equity funding for the Jordan banks if increase in performance by these banks is to be achieved.

The Equity to assets ratio is statistically significant with probability value of 0.000 and the coefficient is (0.86339). The positive coefficient illustrate that for a 1% increase in Equity to assets ratio in Jordan banks return to investors will as well increase by 0.86 units. Liquidity adequacy ratio is statistically significant at 0.0041 however the coefficient of (-0.020313) shows that there is a negative relationship between Liquidity adequacy and return on equity and when liquidity increase by 1% return on equity falls by 0.020 units. The loan to deposit ratio is statistically insignificant and the coefficient is positive signifying a favourable relationship between loan to deposit ratio and return on equity. Bank size is statistically insignificant at 0.6886 with a positive coefficient of 0.000000000000311 showing that an increase in bank size by 1% lease to increase in return to investors by trivial 0.000000000000311 units. Banks in Jordan would implement policies that expand the asset base of bank size should thy want to realise an increase in return to investors.

Summary

The results of the modelled data indicate that the banks in Jordan has to implement different measures in order to increase operation efficiency as measured by the return on assets while on the other hand can increase shareholder value by return on equity.

Results reveal that to increase bank operational performance debt has to be kept lower than equity levels the banks has to strike a balance to increase bank performance. The equity assets ratio when increased increase performance for banks in Jordan. Increasing the bank size through growing the assets base results in increase in bank performance and shareholder value therefore policy makers should focus on growing the bank's assets value to increase performance.

4.CHAPTER: SUMMARY,RECOMMENDATIONS AND CONCLUSIONS

4.1 Introduction

The preceding chapter has laid out scrutinize of the findings of the research; this chapter therefore summarize the study, present a conclusion and finally offer recommendations on the existing impression capital structure on performance of commercial banks profitability.

4.2 Summary

The chief objective of the research was to ascertain the impact of capital structure on the performance of commercial banks in Jordan. To achieve this data was attained from six commercial banks in Jordan for the period 1999 to 2016 giving us 102 observation since some of the data had unit root and was made stationary at 2nd difference. Panel data approximation technique of fixed and random effect model was hired to analyse the data. To ascertain the presentation of commercial bank's, the study hired ROA and ROE since they are the widely utilized determinants of bank performance as per the literature on the topic. As such ROA and ROE were used as the needy variables for the study and bank size, liability to equity ratio, equity to belongings ratio, Liquidity adequacy and Loans to deposits ratio as the explanatory variables.

A widespread literature review of the previous empirical researches was viewed at in chapter 2, and it was seen that for both dependent and explanatory variables such variables adopted by this study were also employed giving credibility to this research. In summary the empirical findings of the effect of capital structure on act of commercial banks in Jordan presented the following impacts. An undesirable impact of liability to equity ratio on the performance of the banks was insignificant, entailing that too much debt is not too good for the profitability of the commercial banks in Jordan, and Loan

to Deposits ratio showed a positive coefficient for both ROA and ROE entailing that loan to deposit ratio has an affirmative impact on the presentation of commercial banks in Jordan but it was an insignificant statistic, also, the bank size was insignificant statistic.

Equity to Assets was statistically significant and had a positive impact on performance of Jordan banks as proved by a positive coefficient of both ROA and ROE. The third explanatory variable was statistically significant liquidity adequacy which presents an adverse implication to both ROA and ROE as measures of Jordan bank performance. The ratio show the liquidity position of banks too high a ratio might mean that the banks have no much liquid assets to cover for unseen circumstance however too low a ratio might as well mean that the profitability of the banks is low.

4.3 Recommendations and Conclusion

Listed underneath are some recommendations based on the study and results of the research. The research has assisted in uncovering how critical banks and all monetary institutions are to the economic development of a country and the global economy as well; as a result stakeholders for the bank should appreciate the economic powerhouses they are.

Debt do not always improve the financial performance of firms as such it is highly recommended that banks in Jordan should utilize other means to raise finances that is through equity financing , this is so also since a negative impact amid debt to equity ratio and profitability of Jordan banks has been empirically proven. Also a positive impact of loans to deposit ratio for Jordan banks is not much of a favourable situation since, too high of this ratio implies that the banks are not liquidity and less liquidity normally leads to insolvency hence closure of firms, thus the finance managers of banks in Jordan ought to watch out for the ratio.

The study utilized 6 banks as the sample of the banks in Jordan, these were selected basing of them being the six leading banks in terms of capitalisation, also the study focused on the impact of capital structure on profitability of commercial banks in Jordan hence the study was narrowed to only commercial banks. The researcher also observed that in Jordan , Equity to Assets ratio and liquidity adequacy are the only statistical significant variables meaning they have a notable impact to the profitability

of commercial banks in Jordan. Conclusively based on the empirical finds the study concludes that there is significant effect of capital organization on firm performance.

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APPENDIX

Dependent Variable: ROA

Method: Panel Least Squares

Date: 04/10/18 Time: 19:40

Sample (adjusted): 2000 2016

Periods included: 17

Cross-sections included: 6

Total panel (balanced) observations: 102

Variable	Coefficient	Std. Error	t-Statistic	Prob.
DRD1	-0.000750	0.009257	-0.081030	0.9356
EARD1	0.088871	0.017454	5.091631	0.0000
LARD1	-0.022257	0.007372	-3.018933	0.0034
LDD1	6.51E-05	0.000131	0.495005	0.6220
LAGROA	0.724166	0.070763	10.23364	0.0000
SIZE	2.02E-15	5.03E-14	0.040139	0.9681
C	0.003351	0.001139	2.943109	0.0043

Effects Specification

Period fixed (dummy variables)

R-squared	0.755826	Mean dependent var	0.013596
Adjusted R-squared	0.687828	S.D. dependent var	0.005851
S.E. of regression	0.003269	Akaike info criterion	-8.413141
Sum squared resid	0.000844	Schwarz criterion	-7.821235
Log likelihood	452.0702	Hannan-Quinn criter.	-8.173458
F-statistic	11.11542	Durbin-Watson stat	2.109125
Prob(F-statistic)	0.000000		

Dependent Variable: ROE
 Method: Panel EGLS (Period random effects)
 Date: 04/10/18 Time: 21:15
 Sample (adjusted): 2000 2016
 Periods included: 17
 Cross-sections included: 6
 Total panel (balanced) observations: 102
 Swamy and Arora estimator of component variances

Variable	Coefficient	Std. Error	t-Statistic	Prob.
DRD1	0.002713	0.009052	0.299665	0.7651
EARD1	0.086339	0.016616	5.196196	0.0000
LARD1	-0.020313	0.006910	-2.939590	0.0041
LDD1	2.51E-05	0.000128	0.196545	0.8446
SIZED1	3.11E-13	7.74E-13	0.402027	0.6886
LAGROE	0.714465	0.062312	11.46595	0.0000
C	0.003463	0.001037	3.338717	0.0012

Effects Specification		S.D.	Rho
Period random		0.001997	0.2720
Idiosyncratic random		0.003268	0.7280

Weighted Statistics			
R-squared	0.634459	Mean dependent var	0.007552
Adjusted R-squared	0.611372	S.D. dependent var	0.005172
S.E. of regression	0.003224	Sum squared resid	0.000988
F-statistic	27.48147	Durbin-Watson stat	2.166629
Prob(F-statistic)	0.000000		

Unweighted Statistics			
R-squared	0.623437	Mean dependent var	0.013596
Sum squared resid	0.001302	Durbin-Watson stat	2.266943

ETHICS COMMITTEE APPROVAL



04.06.2018

Sayın Raad Abdelhalim Ibrahim Alsakarneh

Bilimsel Araştırmalar Etik Kurulu'na yapmış olduğunuz **“The Impact Of Capital Structure On Financial Performance Of Commercial Banks In Jordan”** başlıklı proje önerisi, sadece ikincil kaynak kullanıldığı için Etik Kuruluruna girmesine gerek yoktur. Bu yazı ile birlikte sadece ikincil kaynak kullanmak şartıyla araştırmaya başlayabilirsiniz.

Doçent Doktor Direnç Kanol

Bilimsel Araştırmalar Etik Kurulu Raportörü

A handwritten signature in black ink, reading "Direnç Kanol".

Not: Eğer bir kuruma resmi bir kabul yazısı sunmak istiyorsanız, Yakın Doğu Üniversitesi Bilimsel Araştırmalar Etik Kurulu'na bu yazı ile başvurup, kurulun başkanının imzasını taşıyan resmi bir yazı temin edebilirsiniz.

04.06.2018

Dear Raad Abdelhalim Ibrahim Alsakarneh

Your project "The Impact Of Capital Structure On Financial Performance Of Commercial Banks In Jordan" has been evaluated. Since only secondary data will be used the project it does not need to go through the ethics committee. You can start your research on the condition that you will use only secondary data.

Assoc. Prof. Dr. Direnç Kanol

Rapporteur of the Scientific Research Ethics Committee

Direnç Kanol

Note: If you need to provide an official letter to an institution with the signature of the Head of NEU Scientific Research Ethics Committee, please apply to the secretariat of the ethics committee by showing this document.

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