

Abstract

In contrast to the existing literature and empirical studies on optimal leverage and speed of adjustment in the United States of America and other developed countries, this thesis intends to investigate target leverage and the speed of adjustment in a developing economy through a case study of the Indian corporate sector. This study uses the Corrected Least Square Dummy Variable Technique (LSDVC) for unbalanced panel to estimate the optimal leverage and a second stage fixed effects regression for estimation of the speed of adjustment. A diverse sample of 1471 listed manufacturing firms over a fifteen year time period (1996-2010) has been considered for the study. The study finds a moderate speed of adjustment (14%) in the Indian corporate sector, in contrast to the higher speed of 22% as documented in the United States (Flannery and Hankins, 2007). The results confirm that Indian firms engage in active target adjustment regarding optimal leverage.

Keywords:

Target Capital Structure, LSDVC, Speed of Adjustment, India