

## **A Literature Review on Capital Structure, Ownership Structure, and Firm Performance**

### **Revue de la littérature sur la structure du capital, la structure de propriété et la performance des entreprises**

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**Abstract:**

This paper presents a systematic review on the interactions between capital structure, ownership structure, and firm performance, with the aim of identifying key research trends and highlighting gaps in the literature. Drawing on theoretical and empirical contributions published in journals in finance, economics, management, and governance, our study analyzes the mechanisms through which financing choices and ownership structure influence firm performance. The article reveals the existence of heterogeneous empirical results regarding the impact of financial leverage on performance and underscores the growing importance of governance mechanisms, particularly ownership structure, in explaining these divergences. This review contributes to the literature by providing a synthesis of existing research, identifying the main factors explaining the diversity of empirical results, and suggesting several avenues for future research on the interactions between governance, financing, and performance.

**Keywords:** Capital structure, ownership structure, corporate governance, firm performance.

**Résumé :**

Cet article présente une revue systématique sur les interactions entre la structure du capital, la structure de propriété et la performance des entreprises, dans le but d'identifier les principales tendances de la recherche et de mettre en évidence les lacunes de la littérature. S'appuyant sur des contributions théoriques et empiriques publiées dans des revues en finance, économie, gestion et gouvernance, notre étude analyse les mécanismes à travers lesquels les choix de financement et la structure de l'actionnariat influencent la performance des entreprises. L'article révèle l'existence de résultats empiriques hétérogènes concernant l'impact du levier financier sur la performance et souligne l'importance croissante des mécanismes de gouvernance, en particulier la structure de propriété, dans l'explication de ces divergences. Cette revue contribue à la littérature en proposant une synthèse des travaux existants, en identifiant les principaux facteurs expliquant la diversité des résultats empiriques et en suggérant plusieurs pistes de recherche futures concernant les interactions entre gouvernance, financement et performance.

**Mots clés :** Structure du capital, structure de propriété, gouvernance des entreprises, performance.

## Introduction:

Since the groundbreaking paper of Modigliani & Miller (1958), capital structure – defined as the mix of debt and equity used to finance a firm’s investments and operations – has become one of the most important determinants of firm value (Jensen & Meckling, 1976; Myers, 1977; Ross, 1977; Jensen, 1986). At the same time, firm performance has been shown to shape future financing decisions, thus creating a bidirectional relationship between these two elements (Berger & Di Patti, 2006; Margaritis & Psillaki, 2007; Margaritis & Psillaki, 2010).

Although the link between capital structure and performance has been widely studied in the literature, the results remain highly controversial (La Rocca, 2007). While some studies assert that leverage benefits performance (Jensen & Meckling, 1976; Ross, 1977; Al-Najjar & Al-Najjar, 2017; Rao, et al., 2020), others find that indebtedness can lead to financial distress (Doorasamy, 2021; Muhammad, et al, 2021; Sumani & Suryaningsih, 2022). According to La Rocca (2007), this heterogeneity may be due to the lack of attention paid to the interactions between capital structure and other corporate governance variables. This is particularly valid for ownership structure (Berger & Di Patti, 2006).

As a matter of fact, ownership structure, or the distribution of shares among different groups of owners (e.g., managers, families, or institutions), can influence management decisions and, consequently, firm performance (Mahrt-Smith, 2005; Wahba, 2014; Bansal, et al., 2021; Aboagye-Otchere & Boateng, 2023). When ownership and control are separated, agency costs may arise (Shleifer & Vishny, 1997). They particularly increase when managers indulge in perquisites, manipulate inputs or outputs to suit their own preferences, or simply exert insufficient work effort, thereby failing to maximize firm value. In other words, agency costs of outside equity are materialized as the loss of efficiency resulting from managers serving their own interests, rather than trying to maximize firm value. These dynamics suggest that ownership structure is deeply intertwined with firm performance.

In line with corporate governance literature, there is increasing evidence that the interactions between capital structure and ownership structure have an impact on firm performance (Mahrt-Smith, 2005; La Rocca, 2007). This conclusion has also been reached through empirical research (Berger & Di Patti, 2006; Ngatno & Youlianto, 2021; Aboagye-Otchere & Boateng, 2023). However, most studies depict these variables separately, thereby overlooking the bidirectional association between financing decisions and performance outcomes, as well as the role of corporate governance mechanisms in shaping this nexus. This fragmented approach has contributed to inconsistent empirical findings and an incomplete understanding of the mechanisms linking capital structure, ownership, and firm performance. While some studies highlight the disciplining role of leverage on performance, others emphasize the risks associated with excessive debt.

In this context, an important research question emerges: how do capital structure, ownership structure, and firm performance interact within corporate governance mechanisms? The objectives of this study are threefold. First, to review the main theoretical foundations explaining the relationship between capital structure and firm performance. Second, to analyze the role of ownership structure as a corporate governance mechanism influencing firm performance. Third, to identify how ownership structure interacts with financing decisions and

performance outcomes, while highlighting the main research gaps and avenues for future research.

To address our research question, this literature review adopts a systematic approach aimed at synthesizing the main theoretical and empirical contributions examining the interactions between financing policy, ownership structure and firm performance. The review follows a structured process of identification, screening and analysis of relevant studies in order to ensure a rigorous and transparent synthesis of the literature.

The remainder of this article is structured as follows. Section 1 presents the methodology adopted for the literature review. Section 2 reviews and synthesizes the main theoretical and empirical findings on the relationships between capital structure, ownership structure, and firm performance. Section 3 discusses the key insights emerging from the literature, highlighting underlying mechanisms, sources of heterogeneity, and theoretical and methodological implications. The last section concludes.

## 1. Methodology

By adopting a systematic approach, our review aims to synthesize theoretical and empirical studies examining the interplay between capital structure, ownership structure, and firm performance. The objective is to identify dominant findings, methodological trends, and research gaps.

The literature search was conducted following a structured three-step procedure. First, relevant studies were identified through major academic databases, including Scopus, ScienceDirect, and SpringerLink, which are widely recognized for publishing peer-reviewed research in finance, economics, management, and corporate governance. Combinations of the following keywords were used in the search:

- *capital structure, leverage, debt, financing, equity;*
- *ownership, concentration, governance, shareholder, shareholding;*
- *performance, profitability, Tobin's Q, value, return on assets, return on equity.*

Additional relevant studies were identified through backward and forward citation tracking in order to ensure comprehensive coverage of the literature.

Second, the identified studies were screened based on their titles and abstracts in order to exclude articles not directly related to the research topic. The initial search resulted in 120 articles. After removing duplicates and screening titles and abstracts, 29 studies were excluded because they did not directly address the relationship between capital structure, ownership structure and firm performance.

Third, the remaining papers (91 articles) were assessed for eligibility according to predefined inclusion and exclusion criteria before being retained for the final analysis. Articles were included if they examined at least two of the dimensions: capital structure, ownership structure, and firm performance. Papers were excluded if they focused on unrelated topics, lacked measurable financial variables, or were not published in peer-reviewed academic journals. The review mainly studies articles published between 2000 and 2025, while including seminal

theoretical contributions to provide foundational context. Following the screening process, a final set of 61 studies was retained for in-depth analysis.

## 2. Results:

### 2.1. Capital structure and firm performance

At large, a firm's financial resources can be categorized into debt and equity, with capital structure referring to the mix of resources used to finance investments and operations. If mismanaged, the balance between debt and equity can lead firms into financial distress (Eriotis, et al. 2007). This makes capital structure one of the major areas of concern in finance. An extensive literature has been devoted to the core decision of financing policy and its effects on corporate performance (Harris & Raviv 1991; Myers, 2001; Al-Najjar & Al-Najjar, 2017; Bansal, et al., 2021).

The influential paper of Modigliani & Miller (1958) laid the foundation for the literature on capital structure by arguing for the debt irrelevance proposition, according to which a firm's value is independent of its capital structure under perfect market conditions. Many researchers have followed their lead, suggesting different theoretical approaches to solve the puzzle of the relationship between financing choices and firm performance. However, after decades of research, the debate remains unsettled.

Based on the signaling theory, the issuance of debt is seen as a positive signal of a firm's quality and financial health (Ross, 1977), which fosters stakeholders' confidence. Within this framework, the link between debt policy and firm performance is presumed to be positive. In addition, in their agency theory, Jensen & Meckling (1976) introduced the concept of agency conflicts between shareholders and managers. Their work underlines that the interests of stakeholders, in particular managers and shareholders, are not necessarily aligned. Debt has been proposed as a governance mechanism capable of constraining opportunistic behavior by managers, discouraging inefficient resource allocation decisions, and mitigating the costs associated with bankruptcy (Jensen, 1986). This alignment of interests can have a positive impact on performance.

However, when debt is excessively used, the opposite effect may occur. Higher levels of indebtedness have been proven to lead to conflicts of interest between lenders and shareholders (Jensen & Meckling, 1976). Wary of the possibility of managers shifting risk from shareholders to lenders through overinvestment, creditors may demand higher interest rates on loans in order to protect themselves. This dynamic implies that an escalation in debt can lead to higher total agency costs, and consequently eroding performance. Furthermore, Stulz (1990) has demonstrated that debt can mitigate overinvestment problems, but concurrently, it has the potential to aggravate underinvestment issues. Hence, the use of leverage can have a dual impact on profitability, exerting both beneficial and detrimental effects.

Although agency and signaling theories have different perspectives in elucidating the relationship between owners, managers and lenders, they conceptualized these links as monotonic functions operating effectively within a designated space. This suggests that a specific debt level is invariably favored regardless of contextual, structural and institutional variables.

Furthermore, the debate between two main theoretical approaches of capital structure, the trade-off theory (Kraus & Litzenberger, 1973) and the pecking order theory (Myers, 1984; Myers & Majluf, 1984), is still in vogue. The trade-off approach, on the one hand, balances the advantages and disadvantages of debt; while the pecking order theory, on the other hand, highlights that the resources allocation chosen by management follows an order of preference: self-generated earnings, debt, and then new equity issuance.

Table N°1 outlines key capital structure theories in chronological order:

**Table N°1: Evolution of capital structure theories**

<b>Theory</b>	<b>Researcher(s)</b>	<b>Originality / Value</b>
<b>Theory of irrelevance</b>	Modigliani & Miller (1958)	Capital structure has no impact on firm value.
<b>Theory of relevance</b>	Modigliani & Miller (1963)	Capital structure impacts firm value through debt tax shield.
<b>Trade-off theory</b>	Kraus & Litzenberger (1973)	An optimal level of debt exists, it is the level that equalizes tax benefits and the probability of financial distress.
<b>Agency theory</b>	Jensen & Meckling (1976)	Conflicts between agents and principals impact capital structure.
<b>Signaling theory</b>	Ross (1977)	Contrary to issuing equity, debt issuance is perceived as a positive signal of performance.
<b>Pecking order theory</b>	Myers (1984), Myers & Majluf (1984)	In financing their operations and investments, firms prefer retained earnings, then debt, over fresh equity due to information asymmetry between managers and investors.
<b>Stakeholder theory</b>	Titman (1984)	When making capital structure decisions, firms take into account the non-financial stakeholders.
<b>Dynamic trade-off theory</b>	Fischer, et al. (1989)	Firms have target ranges of debt.
<b>Market timing theory</b>	Baker & Wurgler (2002)	Executives issue equity when prices are high, thus attempting to time the market.
<b>Modified pecking order theory</b>	Bontempi (2002)	MPOT includes both trade-off and pecking order models and it is suitable in hybrid systems.
<b>Dynamic pecking order theory</b>	Morellec & Schurhoff (2011)	The pecking order can be influenced by factors such as changes in profitability, investment opportunities, and the level of asymmetric information over time.
<b>Behavioral consistency theory</b>	Cronqvist, et al. (2012)	Managers make corporate leverage choices that are consistent with their personal leverage choices.
<b>Bargaining theory</b>	Chu & Wang (2017)	A customer's capital structure influences the financial decisions of its suppliers.

*Source: authors' own elaboration*

The theories presented in Table N°1 offer complementary perspectives on corporate financing decisions and their implications for performance. A first category of studies, notably agency theory and signaling theory, highlights the disciplinary role of leverage. From this perspective, debt can help improve performance by limiting opportunistic behavior of managers and sending positive signals to investors.

A second category of theories, including the trade-off theory and its dynamic extensions as well as the market timing theory, emphasizes that companies weigh the benefits and costs of debt. According to these approaches, the optimal level of debt depends on factors such as bankruptcy costs, market conditions, and investment opportunities.

A third perspective, based on the pecking order theory and its subsequent developments, emphasizes the role of information asymmetries in financing choices. Companies generally favor self-financing before resorting to debt or issuing new shares, which implies that the most profitable companies can resort to a lower level of debt.

Finally, different approaches, such as stakeholder theory, behavioral consistency theory, and theories of negotiation within supply chains, broaden the analysis by emphasizing the influence of stakeholder relationships and executive characteristics.

Overall, these different theoretical perspectives suggest that the relationship between capital structure and performance cannot be considered as uniform. Rather, it depends on a set of economic, informational, and institutional mechanisms that simultaneously influence financing decisions and performance outcomes.

Along the same lines, empirical studies have yielded equivocal conclusions upon examining the association between debt and performance. Berger & Udell (2006) conducted a study on the relationship between financing choices and banks' performance in the United States. Utilizing profit efficiency as a metric for performance, they reached a conclusion that leverage positively affects firms, a finding that aligns with the agency theory. Building upon this, Vijayakumaran's (2017) article investigated the impact of capital structure as a governance mechanism on firm value, covering a sample of listed industrial firms in China. The authors find this effect to be significantly positive, suggesting that leverage plays a key role in mitigating agency costs of outside equity by constraining managers' opportunistic behaviors.

Similarly, Abdullah & Tursoy (2019) conducted a study on non-financial listed firms in Germany during the period 1993-2006, exploring the effect of leverage on performance under the adoption of IFRS. The results confirm a positive association between capital structure and firm performance, explained by debt tax shield benefits and lower costs of debt issuance compared to equity. Al-Najjar & Al-Najjar (2017) also demonstrated that the value of SMEs in the United Kingdom improves with leverage, in a context marked by financing constraints.

On the other hand, covering a sample of 224 listed companies in Italy, Muhammad, et al. (2021) observe a negative nexus between the choice of debt financing and profitability. Similarly, Sumani & Suryaningsih (2022) concluded that stock market performance declines sharply with debt. Across a diverse set of industries in Mauritius, Seetanah, et al. (2014) empirically assessed the impact of capital structure on performance for the period 2005-2011. The authors observe that high levels of leverage led to developing financial constraints, thereby supporting the

pecking order theory. Using return on assets and return on equity ratios, the paper concludes that firms with lower leverage achieve superior performance.

Doorasamy (2021) studied the relationship between leverage and corporate performance in East African countries. By employing a Generalized Method of Moments estimation technique in conjunction with Tobin's Q as a performance metric, the author demonstrates that firms can increase their value by reducing leverage level, therefore suggesting that debt exerts a deleterious effect on performance. In addition, Boshnak (2023) suggests that in the context of Saudi Stock Exchange firms, while short-term debt, long-term debt, total debt, and debt-to-equity ratios affect return on assets negatively, return on equity and Tobin's Q are reduced by the effect of long term-debt. This implies that high-debt policies tend to weaken performance.

However, there are some studies that reported mixed results. For instance, Abata, et al. (2017) reach the conclusion that, among the JSE listed companies, leverage effect is contingent on the performance measure employed. In consequence, they recommend that firms define their financial objective – whether to maximize ROE or ROA – in order to select an adequate debt and equity mix.

Furthermore, Ahmed, et al. (2023) focused on the moderating role of agency costs in shaping the dynamics between debt and performance in manufacturing firms listed on the Tehran Stock Exchange (TSE) between 2011 and 2019. The empirical findings exhibit that capital structure has a significant negative influence on Return on Assets and Earnings Per Share, yet a positive effect on Tobin's Q, emphasizing the nuanced impact of leverage depending on the performance metric employed. Bawuah (2024), based on a panel of sub-Saharan companies between 2010 and 2020, finds that companies with high long-term debt perform better than companies where debt structure is dominated by short-term debt. Similarly, Aboagye-Otchere & Boateng (2023) show that, in Ghana, the most profitable firms are those that prioritize long-term debt financing.

Table N°2 summarizes the main empirical evidence on the relationship between capital structure and firm performance.

**Table N°2. Empirical evidence on the relationship between capital structure and firm performance**

Author(s)	Country/Region	Period	Sample	Main finding
Berger & Di Patti (2006)	USA	1990s	Banks	Positive effect of leverage
Margaritis & Psillaki (2007)	New Zealand	2000s	Industrial firms	Positive effect of leverage
Abdullah & Tursoy (2019)	Germany	1993-2016	Non-financial listed firms	Positive effect of leverage
Al-Najjar & Al-Najjar (2017)	UK	2000-2009	SMEs	Positive effect of leverage
Muhammad, et al. (2021)	Italy	2013-2017	Non-financial listed firms	Negative effect of leverage
Doorasamy (2021)	East Africa	2009-2018	Listed firms	Negative effect of leverage
Boshnak (2023)	Saudi Arabia	2016-2019 ; 2020-2022	Listed firms	Negative effect of leverage

Seetanaah, et al. (2014)	Mauritius	2005–2011	Listed firms	Negative effect of leverage
Ahmed, et al. (2023)	Iran	2011–2019	Listed manufacturing firms	Mixed results.
Bawuah (2024)	7 Sub-Saharan African countries	2010–2020	Listed firms	Long-term debt positive, short-term and total debt negative

*Source: authors' own elaboration*

Overall, empirical evidence on the relationship between capital structure and firm performance remains highly heterogeneous and can be broadly grouped into three categories. Several studies support a positive disciplinary role of debt consistent with agency and signaling theories. Others highlight the detrimental effects of excessive leverage through financial distress and agency costs of debt. A third group of papers reports mixed or conditional results, suggesting that the effect of leverage depends on factors such as debt maturity, institutional context, and the performance indicators used.

Therefore, differences between developed and emerging markets, the distinction between short-term and long-term debt, and the performance indicators employed (accounting-based versus market-based measures) significantly influence reported outcomes. Sectoral characteristics may also explain the divergent findings. For instance, financial institutions are subject to regulatory capital requirements, while manufacturing firms often rely more heavily on debt to finance tangible assets. These elements suggest that the leverage–performance nexus is unlikely to be monotonic.

## 2.2. Reverse causality from firm performance to capital structure

Firm performance may also have a bearing on leverage decisions. According to Berger & Di Patti (2006), when firms demonstrate superior performance, they display a propensity to generate higher returns. This enables them to absorb a greater degree of portfolio risk, thereby facilitating the issuance of debt without the concern of bankruptcy. Consequently, efficient companies can afford higher debt levels, since the expectation of higher returns reduces the likelihood of financial distress. This phenomenon is referred to as the substitution effect.

Nevertheless, there is a possibility that firms expecting higher returns choose lower leverage, with the aim of preserving the economic rents or franchise value created by these returns and protecting them from the threat of bankruptcy (Demsetz, 1973; Berger & Di Patti, 2006). Hence, the more efficient a company is, the more likely it is to retain excess equity capital, thus opting for lower debt-to-equity ratios in order to safeguard its future returns or firm value.

Reverse causality from firm performance to capital structure can be explained by the trade-off theory and the pecking order theory. According to the trade-off theory, a high-performing company is able to carry a higher level of debt since it generates stable profits and faces lower bankruptcy risk. A company with high profitability can therefore take full advantage of the tax benefits of interest deductibility while limiting the financial costs associated with debt. Consequently, its optimal debt-to-equity ratio should be relatively high, as it benefits from easier access to debt financing without compromising its financial viability (Fama & French, 2002).

Conversely, from the pecking order theory perspective, successful companies that generate substantial profits do not necessarily need to take on debt. According to this approach, companies first favor internal financing (retained earnings) before considering external financing. A highly profitable company would therefore tend to reduce its use of debt, resulting in a lower debt level (Jarallah, et al., 2019; Doan, 2020).

She & Guo (2018) investigated the reverse causality between corporate performance and financing choices in e-retailing companies. They demonstrated that, in line with the pecking order theory, performance negatively impacts leverage. The authors explain that successful companies have sufficient internal resources to finance their growth and investments, thus avoiding recourse to debt. Similarly, Khafid, et al. (2020) show that high-performing manufacturing firms in Indonesia are reducing their use of debt, and hence the associated costs, such as interests and bankruptcy risk.

On the contrary, Abdullah & Tursoy's (2021) study of German listed companies finds a positive relationship between value and capital structure, showing that the best-performing companies may carry more debt, since they benefit from easier access to external financing. This is because they are perceived by creditors as financially strong. Adhari & Viverita (2015) also identified a positive reverse causality between financial performance and leverage, reinforcing the idea that better performance encourages recourse to debt.

In sum, empirical findings can be grouped into two main patterns. A first group reports positive substitution effects, where highly profitable firms increase leverage due to lower bankruptcy risk. A second group supports the pecking order behavior, where firms rely primarily on internal financing and reduce debt usage as profitability rises. These opposing mechanisms appear to coexist across different institutional settings and stages of financial development. Consequently, capital structure cannot be viewed as an independent determinant of performance but rather as part of a simultaneous adjustment process in which profitability, risk, and financing capacity interact continuously.

### **2.3. Ownership structure and firm performance**

Corporate governance is the set of rules governing the way companies are controlled and managed. It defines the rights and obligations of the various stakeholders involved in a firm and establishes decision-making procedures. In fact, the overarching objective of corporate governance is to mitigate agency problems between principals and agents by ensuring that opportunistic behaviors do not arise (Jensen, 1986).

The concept of corporate governance is broad in scope and significance, yet its delineation is intricate due to the numerous dimensions it encompasses (Ararat, et al., 2021; Dissanayake, et al., 2024). According to Berger & Di Patti (2006), ownership structure stands out as a critical governance variable that should be included in agency cost studies. In the event of its exclusion, testing the relationship between capital structure and performance may be subject to bias, as separation of ownership and control constitutes an essential component of agency costs.

While many studies (Demsetz, 1983; Shleifer & Vishny, 1986; Hu & Zhou, 2008; Rathnayake, et al., 2019) suggest a direct link between firm performance and ownership structure, others (McConnell & Servaes, 1995; Davies, et al., 2005; Poutziouris, et al., 2015) describe this nexus as non-monotonic. In contrast, some researchers (Demsetz & Lehn, 1985; Himmelberg, et al.,

1999; Demsetz & Villalonga, 2001) find no association between ownership structure policy and performance.

The first study of the relationship between ownership structure and firm performance dates back to Berle & Means (1932), who emphasized challenges of separating ownership from control. In large US listed companies, shareholders (owners) often lose direct control over day-to-day management operations, which are left to professional managers (insiders). This leads to agency conflicts where managers may act following their own interests, potentially causing firms to underperform. Jensen & Meckling (1976) extended this discussion by developing the formal principal-agent problem. They asserted that managerial ownership can act as a means of aligning the interests of managers and shareholders, thereby mitigating agency issues.

Nonetheless, Demsetz (1983) pointed out the potentially negative effects of high levels of management ownership. He advocates that while insider shareholding can reduce agency conflicts, it can also have an opposite effect, known as entrenchment. This non-monotonic relationship was further explored by Morck, et al. (1988), who identified an inverted U-shaped link between managerial ownership and firm performance. At low levels of ownership, performance tends to increase with managerial involvement, but it declines when managerial ownership exceeds a certain level and the entrenchment effect becomes significant.

Shleifer & Vishny (1986) showed that the presence of large shareholders (such as families or institutions) can reinforce management oversight, ensuring its decisions are aligned with shareholders' interests. Nevertheless, they warned that even large shareholders can pursue self-serving objectives to the detriment of minority shareholders. Nuancing this perspective, Claessens, et al. (2002) argued that the net effect of concentrated ownership depends on the balance between positive monitoring effects and negative entrenchment effects. When large shareholders monitor management to improve performance, this benefits all shareholders. However, a strong entrenchment effect can harm both the firm's performance and the interests of minority shareholders.

Cornett, et al. (2007) advocate that the presence of large institutional investors improves governance through rigorous monitoring of management, particularly in the banking sector. Nevertheless, institutional investors may sometimes lack the motive to engage in active oversight or may even cooperate with managers if their interests are aligned. Along the same lines, Kabir Saleh, et al. (2022) document, in Chad, that the presence of institutional investors has a negative effect on performance.

Enriching the debate, Villalonga & Amit (2006) brought in other perspectives into how family involvement affects firm performance. They suggest that family ownership can be beneficial, but excessive bureaucracy control structures and incompetent family management are detrimental to firm value. Anderson & Reeb (2003) echoed these findings, arguing that family firms benefit from a lower cost of capital and better operating performance, while cautioning against the risk of family entrenchment. Similarly, Maury (2006) further demonstrates that family ownership can enhance performance in a European context, depending on the degree of family involvement in management. Poutziouris, et al. (2015) depict a non-monotonic relationship between family ownership and firm performance in UK listed companies. They observe that family involvement has a positive effect on performance up to an ownership threshold of 31%, at which point it begins to decline.

La Porta, et al. (2002) added a contextual perspective to the literature studying ownership and performance, showing that corporate governance is highly dependent on a country's legal and institutional framework. Companies in countries with weaker investor protection tend to exhibit higher ownership concentration, often in the form of family shareholding. This concentration can intensify agency conflicts between majority and minority shareholders.

Overall, empirical research on the relationship between shareholding and firm performance reveals three main patterns. A first group highlights a monitoring effect, where managerial, family, or institutional ownership can mitigate agency conflicts by aligning incentives and strengthening oversight. A second group emphasizes entrenchment effects, where excessive control often leads to expropriation of minority shareholders and reduced firm performance. The frequently observed non-linear relationships by a third stream of research, particularly the inverted U-shaped patterns, suggest the coexistence of incentive and entrenchment mechanisms.

Moreover, institutional and legal environments play a decisive role in shaping these effects, as stronger investor protection frameworks tend to enhance the benefits of concentrated ownership while limiting opportunistic behavior. Findings demonstrate that ownership structure does not exert a uniform impact on performance, but operates through complex governance channels that vary across institutional contexts and levels of concentration.

#### **2.4. Capital structure, ownership structure, and performance**

Studies show that ownership structure can also play an important role in shaping financing decisions. Grossman & Hart (1982) argue that in presence of external blockholders, the use of debt can serve as a governance mechanism to bring interests of managers and shareholders together, by reducing available resources for non-value maximizing activities. This implies that the presence of external blockholders often encourages higher leverage ratios. Similarly, Anderson, et al. (2003) posit that family-owned firms may also hold important debt levels, as lenders perceive them as less risky. Since families are often more prudent and directly involved in management, they have a personal interest in maintaining stable performance, which reduces creditors' concerns about managerial opportunism.

Conversely, managerial ownership frequently results in a preference for lower levels of debt, as indebtedness increases the likelihood of bankruptcy, which could jeopardize managers' position or personal wealth invested in the company, known as the non-diversifiable human capital (Friend & Lang, 1988). Brailsford, et al. (2002) added nuance to the relationship between managerial ownership and capital structure by identifying a non-monotonic effect: at low levels of ownership, managers have a motive to use leverage to maximize share value, but they become more conservative as ownership increases to avoid significant financial risks.

Some recent studies examine the interdependencies between financing decisions, ownership structure, and firm performance. Mansour, et al. (2022) studied the moderating effect of capital structure in the relationship between corporate governance quality and firm performance in Jordanian listed companies. The paper posits that robust corporate governance is positively related to performance, with capital structure reinforcing this relationship. Thus, firms can improve performance through good governance while adopting an appropriate debt-to-equity mix.

In Mauritius, Ronoowah & Seetanah (2023) observe a positive bidirectional relationship between firm performance and capital structure. They also show that governance mechanisms and leverage jointly enhance performance, while corporate governance quality and performance together influence capital structure decisions. Harmono, et al. (2023) focus on a sample of manufacturing firms in Asia and argue that leverage partially mediates the relationship between ownership structure and firm value.

Similarly, Ngatno & Youlianto (2021) prove that, in Indonesia, governance mechanisms moderate the impact of capital structure on profitability. Along the same lines, Sumani & Suryaningsih (2022), based on an American sample, observe that good governance reinforces the leverage-performance nexus. Bansal, et al. (2021) also confirm, in India, that state ownership significantly intensifies the leverage-performance relationship, asserting that shareholding influences how debt affects profitability. Pham & Nguyen (2019) came to a similar conclusion for Vietnamese companies using a 2SLS IV method. Aboagye-Otchere & Boateng (2023) also argue, in Ghana, that ownership structure can increase the sensitivity of performance to leverage.

Table N°3 summarizes the main empirical evidence on the relationship between capital structure, governance variables, and firm performance.

**Table N°3. Empirical evidence on the nexus between capital structure, governance variables, and firm performance**

Author (s)	Country/Region	Period	Sample	Governance variable	Role identified	Main conclusion
Mansour, et al. (2022)	Jordan	2014-2019	Listed firms	Governance quality	Moderation	Leverage strengthens the governance-performance link
Ngatno & Youlianto (2021)	Indonesia	2000s	Micro-financial institutions	Governance mechanisms	Moderation	Governance moderates leverage-performance
Pham & Nguyen (2019)	Vietnam	2011-2015	Listed firms	Governance mechanisms	Moderation	Governance affects leverage-performance
Harmono, et al. (2023)	Asia	2014-2018	Manufacturing firms	Ownership structure	Mediation	Leverage mediates ownership-value
Ronoowah & Seetanah (2023)	Mauritius	2009-2019	Listed firms	Governance + leverage	Simultaneous	Dynamic and interdependent relationships
Aboagye-Otchere & Boateng (2023)	Ghana	2010-2021	Non-financial listed companies	Ownership type	Moderation	Ownership amplifies performance sensitivity to leverage

*Source: authors' own elaboration*

Overall, the literature highlights three main analytical mechanisms linking ownership structure, financing decisions, and firm performance. First, ownership structure can moderate the relationship between leverage and firm performance by shaping managerial incentives and monitoring intensity. Second, capital structure may mediate the nexus between ownership structure and performance through financing decisions and risk exposure. A third group of studies highlights simultaneous or dynamic relationships, suggesting that leverage, governance mechanisms and firm performance adjust jointly over time. These findings suggest that ignoring governance variables leads to incomplete and potentially biased conclusions. However, despite the growing interest in interaction models, the literature remains fragmented, with limited consensus on the magnitude and direction of these effects across institutional contexts.

### 3. Discussion

This literature review illustrates the growing interest in understanding how capital structure, ownership structure, and firm performance interact. Rather than operating as independent mechanisms, these dimensions appear increasingly interconnected, shaping firms' ability to generate sustainable performance. Over time, research has moved away from simple linear relationships toward more nuanced perspectives that recognize governance effects.

One of the most striking features of the existing literature is the diversity of empirical results regarding the impact of leverage on firm performance. While several studies emphasize the disciplining role of debt in reducing agency problems and improving efficiency, others show that high levels of leverage expose firms to financial distress and operational rigidity. These contrasting outcomes suggest that debt is neither inherently beneficial nor systematically harmful. Instead, its impact depends on the economic environment, firms' access to financing, and the governance mechanisms that shape managerial decision-making.

A growing number of contributions also acknowledge that performance itself influences capital structure choices. Firms may increase borrowing when performance improves, but they may also rely more heavily on internal resources to preserve franchise value. This reciprocal relationship highlights the dynamic nature of financing decisions and challenges traditional approaches that treat leverage as an exogenous determinant of performance. Nevertheless, many empirical studies continue to adopt simplified modeling strategies (static models) that struggle to fully capture these feedback effects.

Governance mechanisms, in particular ownership structure, further enrich this debate by revealing how control and incentives shape performance outcomes and financing policies. Concentrated ownership, family involvement, institutional, and managerial shareholding can strengthen monitoring and align interests, yet excessive control often leads to entrenchment and reduced value creation. The frequent observation of non-linear effects reflects this dual role of ownership as both an efficient governance tool and a potential source of conflict. However, much of the literature focuses on ownership categories without adequately considering the degree of control concentration, which may contribute to the persistence of mixed findings.

Recent research increasingly points to the importance of governance mechanisms in moderating the relationship between leverage and performance. Rather than influencing corporate outcomes independently, ownership structure shapes how effectively debt contributes to

performance. In some contexts, strong governance enhances the disciplinary role of leverage; while in others, weak oversight amplifies financial risk. Despite this progress, interaction-based approaches remain relatively limited, particularly outside a small number of institutional settings.

Beyond these core relationships, several broader factors remain insufficiently explored in the existing literature. Macroeconomic volatility, financial crises, and institutional quality shape firms' access to external financing, risk exposure, and adjustment speed (Oztekin & Flannery, 2012; Cook & Tang, 2010), thereby influencing both leverage choices and performance outcomes. Yet, most capital structure studies implicitly assume stable economic environments and overlook how fluctuations in interest rates, credit supply constraints, or economic downturns modify the effectiveness of debt as a governance mechanism. Incorporating macro-financial conditions would therefore provide a more realistic understanding of why similar leverage levels produce divergent performance effects across periods and countries.

In addition, emerging concerns related to sustainability practices increasingly affect corporate financing and valuation, as firms with stronger environmental and social performance tend to exhibit greater resilience and lower risk exposure (Albuquerque & Zhang, 2020; Bolton & Kacperczyk, 2021). Despite this growing relevance, ESG dimensions remain largely disconnected from traditional capital structure and ownership structure analyses. Understanding how ownership concentration influences the integration of sustainability objectives into financing strategies could help clarify the governance channels through which long-term value is created.

Other gaps were also highlighted through this review. Most studies focus on listed firms due to data availability, despite the fact that unlisted firms differ substantially in ownership concentration, governance structures, and financing constraints (Asker, et al., 2015). This bias may limit the generalizability of existing findings and understate the role of concentrated control typical of private firms. Moreover, leverage is frequently measured in aggregate terms, overlooking differences in debt type, maturity, and creditor structure that imply distinct monitoring and risk effects (Colla, et al., 2013). Accounting for debt composition could help explain the heterogeneity observed in leverage–performance relationships. Variations in legal systems, financial development, and investor protection can also significantly shape financing and governance outcomes across countries (De Jong, et al., 2008; Fan, et al., 2012). Broader cross-country analyses incorporating institutional factors remain necessary to better understand these contextual influences.

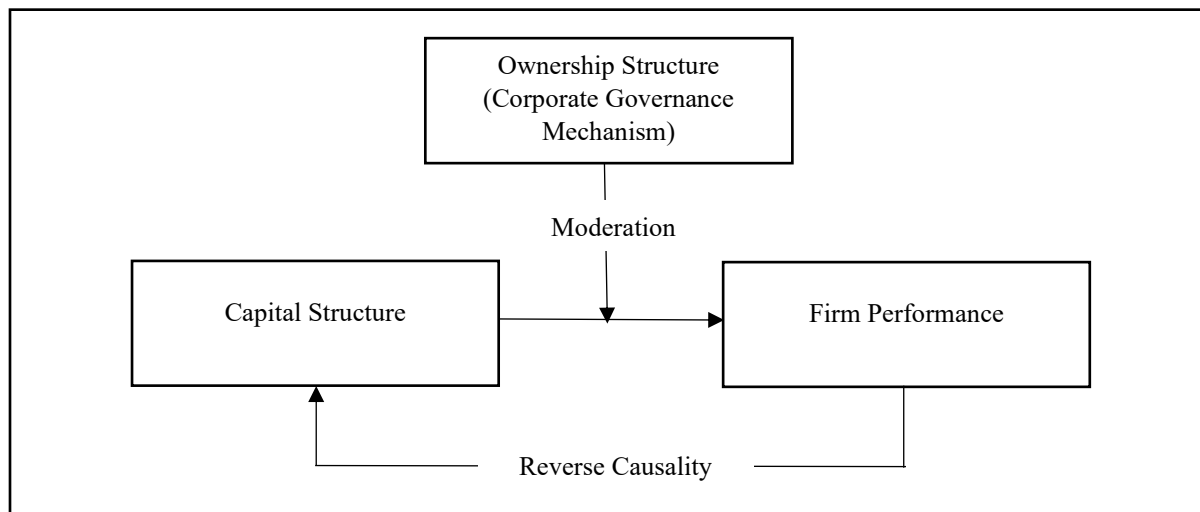
From this perspective, the empirical results reported in the literature can be grouped into several analytical configurations. A first category of studies highlights a positive effect of debt on performance, generally interpreted through its disciplinary role in reducing agency conflicts. A second category, on the contrary, highlights the potential negative effects of debt, particularly those related to the costs of financial distress and conflicts of interest between shareholders and creditors. A third category highlights more nuanced results, suggesting that the relationship between capital structure and performance depends on contextual factors such as ownership structure, debt composition, performance indicators used, and the institutional or sectoral environment.

In light of the theoretical and empirical contributions analyzed in this review, the relationships between capital structure, ownership structure, and corporate performance can be summarized

through an integrated conceptual framework. The literature suggests that capital structure influences corporate performance through various mechanisms, including the disciplinary effects of debt highlighted by agency theory and signaling effects. At the same time, several studies highlight an inverse causal relationship, whereby financial performance can also influence corporate financing decisions, in line with the predictions of the trade-off and the pecking order theories. In addition, ownership structure appears to be a key governance mechanism that can modulate the relationship between debt and performance.

Figure N°1 provides a summary of these various interactions by presenting an integrated conceptual model of the relationships between capital structure, ownership structure, and corporate performance.

**Figure N°1: Conceptual model of the relationships between capital structure, ownership structure, and firm performance**



*Source: Authors' own elaboration*

Taken together, the evidence suggests that the fragmented nature of current research partly explains the persistent lack of consensus in empirical findings. Capital structure theories, governance mechanisms, and institutional factors interact in ways that cannot be fully captured through isolated or static frameworks. A more integrated approach—one that recognizes dynamic adjustments, ownership incentives, and contextual influences—appears necessary to advance the understanding of how financing decisions and governance structures jointly shape firm performance.

## Conclusion

Our review emphasizes the importance of considering the interactions between corporate governance variables in order to fully fathom the relationship between financing decisions and firm performance. The latter interdependencies, even after decades of research, remain a topic of significant debate among researchers and practitioners.

Despite the richness of existing research, this article reveals several persistent limitations that contribute to the lack of consensus in empirical findings. The literature remains largely fragmented, often examining financing decisions, shareholding structure, and firm performance

in isolation while insufficiently capturing their dynamic and interdependent nature. Methodological simplifications, particularly the widespread use of static models and aggregate leverage measures, further constrain empirical interpretations. In addition, the predominance of studies on listed firms and developed economies limits the generalizability of results, while institutional heterogeneity across countries remains underexplored. Emerging dimensions such as governance variables interactions, macro-financial conditions and sustainability considerations also remain peripheral in most analyses. Addressing these gaps through more integrated, dynamic, and context-sensitive frameworks represents a critical avenue for advancing understanding in this field.

This literature review provides useful contributions and highlights persistent gaps in the literature. However, to further deepen the understanding of these interactions, future reviews could adopt meta-analyses or cross-country comparisons.

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