International Journal of Innovation, Creativity and Change. www.ijicc.net
Volume 15, Issue 5, 2021

# Effect of Asset Utilisation and Corporate Growth on Financial Performance

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This study examines the effects of asset utilisation and corporate growth on financial performance by using the sample dataset of 30 listed textile companies on the Pakistan Stock Exchange from 2015 to 2019. The study incurred that asset utilisation influences the financial performance of the company before any investment decision is made. By using descriptive statistic and panel regression techniques, the results show that asset utilisation and corporate growth have a significant and positive influence on financial performance. The results of this study also indicate random effect model as a best fit. This study expects to provide a better understanding of the asset utilisation and the role of corporate growth in the company in defining the financial performance of the company. The findings of the study help in supporting the arguments of leverage irrelevance theory and pecking order theory which help in improvement of financial performance.

**Keywords:** *Asset Utilisation, Corporate Growth, Financial Performance, Size*

## 1. INTRODUCTION

Finance is a process of increasing capital or funds for every kind of expense. Governments, consumers and business firms mostly do not have the funds which are available for expenditure, paying debt, or for completing other transactions. They must have to sell equity or borrow the money which is needed by them for conducting the operations. Investors and savers accumulate funds on the other hand, which could earn dividends or interest to put them into productive use. The company owners expect the company to have the ability to better maintain sustainable development and also increase the amount of company assets while running the enterprises. Financial intermediaries are the institutions that channel the funds from the saver to the users. These institutions include savings banks, commercial banks, savings and loan associations and also non-bank institutions like insurance companies, credit unions, investment companies, pension funds, and financial companies.

The company uses private debt and equity at the same time, which includes long and short-term debts, to fund the company's operational activities for utilising the assets of the company which are being determined. The board managers are in charge of the decision-making of asset utilisation as they are also required to uphold the operational activities of the company.

Financial performance is a key criterion through which many investors and creditors tend to form the basis of their economic decisions and assess the firm's and manager's performance.
The measurement of financial performance is based on many decisions which include stock prices, executive compensation, stock risk, investment-related decisions, and other cases stated by Azarbaijani (2011). The companies are established for improving the wealth of shareholders with the improvement in the corporate market value. The manager's board is trusted to manage the company for obtaining the profits which eventually helps in the increase in the company owners' wealth. The investment choices determine what sum of assets are to be consumed on the operational activities of the company. These operational activities then consume the assets to increase sales and to increase profit, which increases the wealth of the owners of the company. The asset utilisation of the company is most significant as it helps in achieving the goals of the company. The company can achieve corporate growth through the gradual expanding procedures of the enterprise, diversification, development of the product, growing the number of workers, increasing the assets and profit of the firm, and improving sales. Vijayakumar (2011) indicated that corporate growth increases the sales of the company and the asset and profit development of the company. The continuous attempts that are made by the company in managing and utilising the resources result in financial performance.

The textile industry in Pakistan has a huge contribution in the gross domestic product and is known as the biggest industry in the country. The capital structure of any sector has a big effect on the financial performance of that sector. The utilisation of the assets is also linked with the size of the firm they are applying their strategies to. Due to the lack of financial performance increasing measures in Pakistan, despite lying among the biggest industries, the textile industry of Pakistan still cannot manage to generate the revenues it should be generating. The financial performance is not the way it should be for such a big industry and so the same goes for asset utilisation. The aim of this research is to dig through these perspectives and find measures so that we will be contributing to the improvement of the asset utilisation and corporate growth impact on the financial performance of the industry.

## 1.1 PROBLEM IDENTIFICATION

In Pakistan, the assets are not utilised very well because of the lack of responsibility, lack of resources, and sick ethical manner. Lack of financial resources to run the operations by any firm regardless of its size and the fixed asset turnover (which leads to the efficiency of the firm to employ its fixed assets to generate sales) may lead the firm to face difficulties and have a negative impact on the financial performance of the firm, as stated by Junaid et al. (2020).

For corporate growth, a firm may need to determine its capital structure. It may require internal or external funding depending upon its capital structure and requirement of funding its operations. In that connection, pecking order theory states the internal factors like the risks and capabilities of the firm in order to select the method of financing. The internal funding includes the retained earnings of which a firm can use for opportunities for reinvestment, this type of fund helps the firm in the growth of capital. In Pakistan, the conditions of the textile industry are not good due to which the utilisation of assets and corporate growth is not done in a useful manner which results in a decrease in financial performance. It is important to have a better understanding of asset utilisation and capital growth and how to increase the profits and sales of the firm.

The research novelty can be seen in the system of the involvement of the asset utilisation that has influences on corporate growth and financial performance. These variables have not been studied in the textile industry of Pakistan before. The underlying research is helpful for the local textile industry in utilising assets in an efficient way which can help in increasing the financial performance of the firm. The utilisation of an asset can determine the financial performance of a company. This utilisation of the assets of the company also states the use of the assets of the company to fund the activities which are operational.

## 1.2 RESEARCH QUESTIONS

- What is the impact of asset utilisation on financial performance in the Pakistan textile sector?
- What is the impact of corporate growth on financial performance in the Pakistan textile sector?

### 1.3 RESEARCH OBJECTIVES

- To determine the impact of asset utilisation on financial performance in the textile sector of Pakistan.
- To analyse the impact of corporate growth on financial performance in the textile sector of Pakistan.

## 2. LITERATURE REVIEW

### 2.1 THEORETICAL FRAMEWORK

#### 2.1.1 LEVERAGE IRRELEVANCE THEORY

Leverage irrelevance theory clarifies that financial performance is resolute by the achievement in the investment which the firm makes. The investment success cannot be parted by the company assets utilisation in the funding of the operational activities which also includes the making of the services and products which gives the company its profit or income. Income from the sale of the firm enhances the company owner's wealth. So, the objective of the firm's utilisation of assets is earning a higher profit which ultimately increases financial performance. Therefore, the investment decisions taken and the company asset utilisation both have a key role in company's success in terms of profitability and financial performance. This theory proposes that deciding on investment and asset utilisation regulate the performance of the company and have an influence on corporate growth. Leverage irrelevance theory says that the choice of investment defines the amount of income. The decision of investment considers amount, type, place, and timing while making the investment. When an investment is made, after that the company must have a focus on improving the process of production by utilising assets effectively.

#### 2.1.2 PECKING ORDER THEORY

Pecking order theory states the imperative ideal of use of resources of the fund for considering the paying cost and helps to control the mechanism of funding. According to the theory, internal funds are the first consideration because they do not cost anyting. The use of the debts is second because they have a lesser cost and choice which lastly should be the issuance of the new shares because they have a greater cost. The corporate growth of the company defines the expected amount of profit of the company. Besides, corporate growth increases profitability which is a sign of financial performance. Kouser (2012) states that corporate growth has a positive effect on profitability. Also, Jang (2011) believed that the development in corporate growth enhances profitability at the same time. There is a theoretical association that when the corporate growth of the company increases, it improves the financial performance of the company.

## 2.2 EMPIRICAL REVIEW

### 2.2.1 ASSET UTILISATION

According to Nkechi & Sunday (2020), asset utilisation has a significant effect on the net worth of big cap companies. To improve the capital structure, companies have to achieve high asset utilisation and also the profit margin which can be attained by the sales growth. A study conducted by Bukit et al. (2018) indicates that asset utilisation has a positive and significant effect on firm value. With a higher ratio of profitability, the higher profit income will be shared to the shareholders and the company value will increase. A severe recession can make highly levered firms increase their asset utilisation to avoid bankruptcy. The relationship between leverage and asset utilisation will enhance the ability of decision-making of the policymakers of the company as according to Pham (2020) effective asset utilization may increase the value of the firm and in an earlier study, Modigliani and Miller (1953) found that the value of the firm is not related with the capital structure. However, in a later study by Modigliani and Miller in 1963, it was found that the value of the firm is greater with debt as compared to without having debt.
Research study conducted by filbeck and Gorman (2000) found that a firm's capital structure is positively related to the asset utilization. It is due to the fact that the firm uses debt for more effective asset utilization.

### 2.2.2 FINANCIAL PERFORMANCE

Financial performance indicates whether the firm is utilising the investment on its assets well or not. Return on assets and return on equity are the main indicators of financial performance. The return on assets is measured by dividing the amount of net income with the total assets. Gunadi et al. (2020) checked the impact of capital structure and firm's size on growth of firm's value by using the financial performance of the firm.

Agency theory describes that there are two participants, one is an agent and another is principal. Both parties have a trust based/fiduciary relationship towards each other.Some researchers criticize it as a controversial theory because it makes many problems in an organisation like self-interested behavior between two groups such as managers and stakeholders, although the stakeholders have less information about the performance compared to the firm manager's, as insisted by Shehata (2014). Also, liquidity, solvency and profitability ratios affect the firm's financial performance. Furthermore, greater liquidity indicates that the firm is in a stable position, while greater leverage is an indication of warning that the firm is in a risky position. Therefore, the point is that the greater the risk, the more return you can expect. As Li (2021) said, the positive impact on financial performance is due to re-structuring of assets to increase their utilisation. The aim of financial firms is to minimise the risks to achieve profit and to earn acceptable returns. Generally, the measures of financial performance are from risk and return. Financial performance decisions are only the operational ability and operational performance which may directly affect the durability of the firm as stated by Chien (2014). The achievement of a company depends on the appropriate component like share in the market, devaluation of cost, and profit. Moreover, there are various indicators that can be used to assess the performance of a firm. For instance, a research study used financial ratios that include assets management, size of assets and equity management to measure the financial performance of the commercial banks in Oman. (Khan & Al Makhtoumi, 2021).

### 2.2.3 CORPORATE GROWTH

Kinasih et al. (2020) focused on sustainability of corporate growth through better utilisation of assets and proper working capital management. The governance of a firm is measured by the many factors, which will affect performance investigation aims and approaches, the business risk, cash flow, and leverage. While comparing the financial patterns between countries, some authors in their papers have inspected the effect of different patterns of corporate finance on economic growth.

Previous research studies by Oppong-boakye et al. (2013) and Rahayu (2018) clarified that corporate growth shows a key part in improving the market value of companies. Equally, external and internal development of the business should be considered as opportunities of investment in the future. Businesses with high growth potential are capable of providing positive signals for their future. Putri & Rahyuda (2020) elaborated the positive effect of capital structure and sales growth on value of the firm. The greater corporate growth and higher number of investments may take long period to achieve the desired outcome. A firm may not generate an acceptable number of products in a short time, still, it will generate greater revenue in the planned period. In that connection the use of long term debt, for the purpose of obtaining short term solutions may seem favourable. These short term solutions may be in the form of asset growth and short-term financing. Size is an important factor of profitability and there have been very few studies that discuss the relationship. Moreover, corporate growth is a key indicator that shows the positive movement of business activities in the company in a certain period and improvement in the business. It causes the investor to think that the company is a potential investment opportunity. Therefore, the increase in investments shall lead to increase in profitability and increase in the firm.

## 2.3 THE INFLUENCE OF CORPORATE GROWTH ON FINANCIAL PERFORMANCE

Çoban (2014) narrated that better corporate growth shows that the firm controls the broad markets, is obtaining higher corporate profit, and is make higher sales. The income hypothesis, which is permanent, shows that the supposed outcome is to be achieved in the future period. This uses the current assets number which is to be used in the funding of the company. The exact amount of profit expected can be attained by increasing financing which results in giving enough income and can improve the future corporate market value. Adi et al. (2013) stated improvements in financial performance increases the market value of firm. Moreover, corporate growth increases the profit that is a sign of the corporate financial act or outcomes (Kouser et al., 2012).

Financial performance is the outcome of the regular experiment made by a firm in applying and handling its income in a more direct and useful way to accomplish the positive objective. The symbol of financial performance combines return on asset, return on equity, and net profit margin. The return of asset follows the capacity of a firm to conduct its assets to attain greater total revenue for an improved corporate financial capability to generate investment in the project which are examined by Barakat (2014). Ullah et al. (2020) discussed that sales growth has a reasonable positive impact on financial performance.

## 2.4 THE INFLUENCE OF ASSET UTILISATION ON FINANCIAL PERFORMANCE

The improvement of asset utilisation of the company advances the financial performance. When asset management is efficient, sales improve, which also improves the profit. The company's capability is to manage the assets to determine the sales increase. The higher sales take out the higher profit which increases financial performance. Excess use of assets of a company imitates the efficiency and effectiveness in the management of the assets and decreases the expenses, which leads to higher profits and an increase in the wealth of the company owners.

Dhandapani & Babu (2013) concluded that there is a need for improvement in the financial performance by creating the different forms of rebuilding, which includes the writing off of lost assets and alteration of the share capital. Fixed assets are the assets that are utilised as a part of the production of godsend services or the supply of goods and services which are to be utilised within a fiscal year. Arbidane and Zelgavle (2012) found that the current assets, their indicators, and the company structures to the larger extent are highly influenced by the situation. Under stable economic conditions, stable development in the companies is observed. As the main concern is the efficiency in the utilisation of assets and the components of the working capital, the performance of the manmade textile industry is much better than the cotton industry.

## 2.5 HYPOTHESIS STATEMENT

This study measures the impact of asset utilisation and corporate growth on the financial performance of a company with the designed hypotheses which are:

**H1:** *The corporate growth of a company has a significant influence on financial performance.*
**H2:** *The asset utilisation of a company significantly influences financial performance.*

## 3. METHODOLOGY

This chapter of the research composes the details of the tools of the methodology which are used for the making of scientific inquiry to get the answers to the research questions.

### 3.1 DATA COLLECTION

The approach which has been used for the study is a quantitative approach. The nature of the study is explanatory as the research is intended to examine the links between financial performance, asset utilisation, and corporate growth. The data that is collected to conduct this study is secondary data. The study data has been collected from the Pakistan Stock Exchange (PSX) of thirty (30) textile companies. Based on convenience sampling, the data has been collected from time span between 2015 to 2019. The software Eviews has been used for the analysis to evaluate and obtain the results for the study. The statistical technique Panel Data Regression has been used for the analysis and for the purpose of attaining the research objectives.

### 3.2 ECONOMETRIC MODEL

$$Financial\ Performance_{it} = \alpha + \beta_1 Corporate\ Growth_{it} + \beta_2\ Asset\ Utilization_{it} + \beta_3 Size_{it} + e$$

-------------------------- Eq.(1)

$$ROE_{it} = \alpha + \beta_1 SALES\ GROWTH_{it} + \beta_2 ASSETS\ GROWTH_{it} + \beta_3 CATO_{it} + \beta_4 ITO_{it} + \beta_5 FATO_{it} + \beta_3 Size_{it} + e$$

### 3.3 VARIABLES

Following are the variables used in the study:

#### 3.3.1 FINANCIAL PERFORMANCE

Financial performance is a dependent variable and return on equity, defined as a measure of financial performance, is calculated by dividing the net income by the shareholder's equity.

$$\text{Return on Equity} = \frac{\text{Net Income}}{\text{Shareholder's Equity}}$$

#### 3.3.2 ASSET UTILISATION

Asset utilisation is an independent variable which specifies the number of assets that are available for use. As suggested by Yulianto (2014), capital asset turnover ratio (CATO), inventory turnover ratio (ITO) and fixed asset turnover ratio (FATO) are the proxies which used to measure the asset utilisation of the available data. The formulas for these ratios are:

$$\text{Capital Asset Turnover} = \frac{\text{Net Sales}}{\text{Average Current Assets}}$$

$$\text{Inventory Turnover} = \frac{\text{Cost of Goods Sold}}{\text{Average Inventory}}$$

$$\text{Fixed Asset Turnover} = \frac{\text{Net Sales}}{\text{Average Fixed Assets}}$$

### 3.3.3 CORPORATE GROWTH

Corporate growth is also an independent variable. Corporate growth increases the sales, assets and profit development of the company. Sales growth and asset growth are the proxies which are being taken to measure the overall corporate growth of the data available (Alfred, 2021).

#### 3.3.3.1 SALE GROWTH

Sales growth is the measure of the previous t year's sale minus current year sales divided by the previous year sales (Alfred, 2021).

= (Sales (n-1) - Sales (n)) / Sales (n-1)

#### 3.3.3.2 ASSET GROWTH

Asset growth is calculated as total assets of the previous year minus total assets of the current year divided by the previous year's total assets (Alfred, 2021).

= (Total Asset (N-1) - Total Asset (n))/ Total Asset (N-1))

### 3.3.4 CONTROL VARIABLE

A size is a control variable is used to keep the results constant while conducting the research. It is a value that is obtained by calculating the natural log of total assets (Allen, 2017).

## 3.4 PANEL DATA REGRESSION

Three basic techniques are employed by the panel data regression and these models talk about the intercept behavior of the study.

1. Common effect model

2. Fixed effect model
3. Random effect model

In panel data analysis, for an appropriate and best model selection, the results of simple equations of OLS with random effect have been evaluated. The Hausman test works as a diagnostic for selecting which model of the available data is applied appropriately. The results show that the P-value of Chi-Square is significant. This indicates that random effect model is the best fit for the study and it also indicates that random effect model should be applied for the further analysis of panel data. Based on the test results, the regression model with the random effect has been considered.

## 4. RESULTS & DISCUSSION

This chapter is composed of results and discussions. These results include the Panel Data Analysis and descriptive statistics.

Table 1: *Descriptive analysis of Textile Companies from 2015 to 2019 (150 Observations)*

| | **Mean** | **Median** | **Maximum** | **Minimum** | **Std. Dev.** | **Skewness** | **Kurtosis** | **Jarque-Bera** | **Probability** |
|---|---|---|---|---|---|---|---|---|---|
| ROE | 2.286 | 1.754 | 11.079 | -18.379 | 2.918 | -2.238 | 21.987 | 2378.4 | 0.000 |
| SALEGROWTH | -0.102 | 0.028 | 0.917 | -9.824 | 0.956 | -7.807 | 75.384 | 34269.7 | 0.000 |
| ASSETGROWTH | -0.013 | 0.0007 | 0.529 | -0.819 | 0.204 | -0.723 | 5.066 | 39.719 | 0.000 |
| CATO | 2.454 | 2.289 | 6.470 | 0.0003 | 1.158 | 0.694 | 4.122 | 19.916 | 0.000 |
| FATO | 2.173 | 2.063 | 7.398 | 0.002 | 1.364 | 0.948 | 4.697 | 40.504 | 0.000 |
| ITO | 6.493 | 4.977 | 37.005 | 0.586 | 4.838 | 3.105 | 17.057 | 1476.02 | 0.000 |
| SIZE | 8.728 | 9.026 | 11.014 | 6.213 | 1.347 | -0.366 | 1.871 | 11.301 | 0.004 |

Table 1 represents the statistical behaviors of the variables which are included in the research. The statistics include the mean, median, mode, skewness & standard deviation

In the above table, the central tendency of roe is 2.23 which means a firm can earn an average of 2.3 and its limit is -18.37 to 11.07. This is the same for the central tendency of sale growth,

-0.102, which means our data shows that most of the companies are suffering a deficiency in sales growth and its limit is -9.82 to .9173. Central tendency of asset growth is -0.0131 which means that the data shows no asset growth in the firm and its limit is -0.8195 to 0.53. In this data, Jarque-Bera shows the normality of data. The result for skewness is mixed. In the table dependent variable ROE, independent variable sales growth and asset growth, and control variable SIZE show negative skewness. The remaining variables reflect positive skewness. overall, the descriptive analysis shows that the data is normal.

Table 2: *Correlated Random Effect – Hausman Test*

| **Test Summary** | **Chi-Sq. Statistic** | **Chi-Sq. d.f.** | **Prob.** |
|---|---|---|---|
| Cross-section random | 4.918600 | 6 | 0.5543 |

Table 2 shows the result of the Hausman Test and Chi-Square shows the significant value which means that random effect is the best fit model and is suitable for analysis of data.

Table 3: *Results of Panel Data Regression with Random Effects*

| **Variable** | **Coefficient** | **Std. Error** | **t-Statistic** | **Prob.** |
|---|---|---|---|---|
| C | -10.12538 | 9.792339 | -1.034010 | 0.3033 |
| SALE_GROWTH | 0.468664 | 0.185495 | 2.526557 | 0.0129 |
| ASSETS_GROWTH | 3.827269 | 1.127615 | 3.394128 | 0.0009 |
| CATO | 1.257850 | 0.278418 | 4.517838 | 0.0000 |
| FATO | 0.555323 | 0.234544 | 2.367675 | 0.0196 |
| ITO | -0.124672 | 0.043534 | -2.863769 | 0.0050 |
| SIZE | 1.034104 | 1.115201 | 0.927280 | 0.3557 |

In table 3, we implement the Cross-Sectional Random Model. The results show that corporate growth (SG p-value 0.012 & AG p-value 0.0009) significantly influences financial performance (ROE). The results show that asset growth (CATO p-value 0.000, FATO p-value 0.019 & ITO p-value 0.005) also significantly influences financial performance (ROE). This model explains that the variation in this data exita as the value of adjusted R2 is 0.57 and the Durbin-Watson Stat is 1.84 which means there is no autocorrelation in the data. The value of F.statistic is 6.87 with the probability value of 0.000 which is significant at a 10% confidence interval.

Table 4: *Effects Specification*

| Statistical Measures | Statistical Values |
|---|---|
| R-Squared | 0.678 |
| Adjusted R-Squared | 0.579 |
| Durbin Watson Statistic | 1.845 |
| F-Statistic | 6.873 |
| Prob (F-Statistics) | 0.00 |

## 4.1 DISCUSSION

The findings of study support Kouser (2012) and Çoban (2014) who also found that corporate growth has a positive and significant influence on financial performance. Ullah et al. (2020) also stated that corporate sales growth positively influences financial performance. The Permanent Income Hypothesis states the income of future expectations define the quantity of the assets to be utilised. The targeted income can be gained by building the increased investments to generate increased future income. Ullah et al. (2020) also concluded that corporate sales growth has a positive influence on profitability. A significant corporate growth shows a high asset of the company which is the main aim of the company. The company's corporate growth fascinates investors for buying shares of that company which results in high stock prices. The study findings support the Permanent Income Hypothesis. This hypothesis states that the expectations of the company of the future profit define the amount of assets to be distributed for the operational activities of the company.

## 5. CONCLUSION

There is a significant and positive influence found between corporate growth and financial performance, with a positive coefficient. It shows that high corporate growth increases the financial performance of a company. There is a guarantee that corporate growth results in high profit in the future and it is a goal to achieve corporate growth through several attempts. To make a company grow to a certain level, the investments are made to have a better capability, to be competitive in the broad economic market and to earn high profits. By improving the corporate growth, the corporate growth can be accelerated to achieve a high financial performance, which helps the company to increase the wealth to the owners of the company. The Permanent Income hypothesis states the income of future expectations defines the quantity of the assets to be utilised. The targeted income can be gained by building the increased investments to generate increased future income. The study findings are the same as Kouser (2012) and Coban (2014) who also found that there is a significant influence of corporate growth on financial performance. A significant corporate growth shows a high asset of the company, which is the main aim of the company. The assets of the company should be utilised most efficiently and effectively because it gives a high profit for the company. A better asset utilisation of the company takes noble guiding and planning to use the assets of the company which includes current assets, fixed assets, and amount of funds that are used for the allocation of the element of assets being used. Leverage irrelevance theory states that the decision of investment defines the corporate profit.

## 5.1 RECOMMENDATIONS

The study expects to support the investors and companies in decision making. The research outcomes give useful recommendations for the companies in proper decision making, efficient asset utilisation, and effective financial policies. This study results in findings such as: first, company corporate growth significantly influences the financial performance. The current investment growth results in higher profits in the future. Second, company asset utilisation has a significant and positive impact on financial performance. Having an insight on the efficiency and effectiveness of the asset utilisation is important for the managers of the company when deliberating on the operational activities of the company. The businesses which efficiently and successfully manage the operational activities can improve profit and reduce costs.

## 5.2 IMPLICATIONS

This study has positive implications for future researchers. This study is a reference for them and other variables like profit growth, total asset turnover, etc. may be explored, which were not addressed in this study. This study can give information for making decisions on finance activities of asset utilisation or policies. This research theoretically can be a contribution to the financial management development and improved process of capital structure decision-making. The decision of capital structure can develop the financial performance which increases the company stakeholders and owner’s welfare. The study results suggest that; first, the opportunity of corporate growth can be utilised to control the funding mechanism if the company must use external funds or internal funds. The most preferred choice for the company is using internal funds as the funds do not add to the debt interest. Second, business threats are a reason which can have a negative impact on the financial performance of the company, so the company should consider the business risk. Third, to decrease the debt interest amount, the companies enhance their asset utilisation with improvement in sales, and efficiently and effectively making the operational activities.

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