A Model of Economic Indicators' Influence on Banks' Capital Structure: Evidence from South Africa

Abstract

This paper examines the influence of economic indicators on South Africa's bank capital structure. The study made use of secondary bank financial data and secondary statistical data for economic indicators from 2000 to 2013. A model is therefore estimated using SmartPLS, a structural equation modelling (SEM) software. With recent global crisis, there has been a huge interest from researchers to study company's capital structure. Numerous studies have conducted empirical investigations on capital structure, but there has not been an intense study in the influence of economic indicators to capital structure. The study specifically explores the South African Banking industry. The capital structure of a firm consists of a particular combination of debt and equity issues to relieve potential pressures on its long-term financing. It is therefore important for banks to make prudent financial decisions to ensure optimal financial performance. This study investigates the impact of economic indicators that include Gross domestic product (GDP), Consumer price index (CPI), Producer price index (PPI), exchange rate, repo rate and unemployment rate on the capital structure of a bank. The SEM results confirmed the simultaneity between capital structure and bank performance as well as between economic indicators and bank performance. The study found that there is a significant positive relationship between capital structure as measured leverage ratio and bank performance. It is envisaged that the research findings will enable banks to make better financial decisions.

Key words

Economic Indicator, capital structure, leverage