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FINANCIAL INCLUSION, CAPITAL STRUCTURE, FINANCIAL DEVELOPMENT AND FIRM PERFORMANCE IN DEVELOPING COUNTRIES

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FINANCIAL INCLUSION, CAPITAL STRUCTURE, FINANCIAL DEVELOPMENT AND FIRM PERFORMANCE IN DEVELOPING COUNTRIES

By

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Thesis Submitted to the School of Graduate Studies, Universiti Putra Malaysia, in Fulfillment of the Requirement for the Degree of Doctor of Philosophy

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DEDICATION

My late father to whom I am much indebted, my loving mother, my caring family, and my helpful brothers and sisters.

My helpful supervisors, especially Dr. Matemilola Bolaji Tunde for his patience, guidance, and encouragement that helped in fostering and carrying out this research.

Abstract of the thesis was presented to the Senate of Universiti Putra Malaysia in fulfillment of the requirement for the degree of Doctor of Philosophy

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The research examined the relationship between financial inclusion, capital structure, financial development, and firm performance using 4642 firms from 22 developing countries between 2010 and 2016. The study aims to achieve three objectives using the system generalized method of moments as the main estimation technique. Firstly, the study investigates financial inclusion as a determinant of capital structure. Secondly, the moderation effect of financial development on the relationship between financial inclusion and capital structure. Thirdly, the moderation effect of financial inclusion on the relationship between capital structure and firm performance.

The two-step system generalized method of moments is applied. The results reveal that financial inclusion is a determinant of capital structure in developing countries and the result are robust to alternative model specifications and different financial inclusion proxy. Financial development also positively moderates the relationship between financial inclusion and capital structure in developing countries. Also, financial inclusion positively moderates the relationship between capital structure and firm performance. The findings imply that financial managers can benefit from raising additional capital as the bank's financial inclusion strategy attract more deposits to lend to firms. Also, shareholders should encourage financial managers to raise debt capital needed to fund positive investment projects from banks whose financial inclusion strategies attract more deposits. Policymakers should enact policies that promote financial market development because such policies would complement the banks' financial inclusion strategies and firms would have more access to debt capital. Lastly, financial managers need to look for ways to access finance and simultaneously maximize the tax-shield benefits of debt in their capital structure that increase firm performance.

The study contributes to the literature in two main ways. Firstly, unlike previous studies that use various dimensional variables to determine capital structure like the firm-specific and country-specific variables; this present study uses financial inclusion variables as the determinant of capital structure. Secondly, the study further explores the moderating effect of financial development on the relationship between financial inclusion and debt; as well as the moderating effect of financial inclusion on the relationship between capital structure and firm performance, which has been overlooked in the capital structure literature.

Abstrak tesis yang dikemukakan kepada Senat Universiti Putra Malaysia sebagai memenuhi keperluan untuk ijazah Doktor Falsafah

KESIMPULAN KEWANGAN, STRUKTUR MODAL, PEMBANGUNAN KEWANGAN DAN PRESTASI FIRM DI NEGARA MEMBANGUN

Oleh

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Penyelidikan mengkaji hubungan di kalangan rangkuman kewangan, struktur modal, pembangunan kewangan dan prestasi firma menggunakan 4642 buah syarikat dari 22 buah negara membangun untuk tempoh 2010-2016. Kajian bertujuan untuk mencapai tiga matlamat menggunakan sistem menggeneralisasi kaedah detik sebagai teknik penganggaran utama. Pertama sekali, kajian menyiasat rangkuman kewangan sebagai satu penentu struktur modal. Kedua, kesan kesederhanaan pembangunan kewangan di hubungan antara rangkuman kewangan dan struktur modal. Ketiga, kesan kesederhanaan rangkuman kewangan di hubungan antara struktur modal dan prestasi firma.

Sistem dua langkah menggeneralisasi kaedah detik diaplikasikan. Keputusan mendedahkan bahawa rangkuman kewangan ialah satu penentu struktur modal di negara membangun dan keputusan teguh kepada spesifikasi model alternatif dan proksi kemasukan kewangan berbeza. Pembangunan kewangan juga secara positif menyederhanakan hubungan antara rangkuman kewangan dan struktur modal di negara membangun. Sebagai tambahan, rangkuman kewangan secara positif menyederhanakan hubungan antara struktur modal dan prestasi firma. Implikasi penemuan pengurus-pengurus kewangan itu boleh memanfaatkan dari meningkatkan modal tambahan apabila bank strategi kemasukan kewangan menarik lebih banyak deposit menguatkan firma. Juga, pemegang saham harus menggalakkan pengurus-pengurus kewangan untuk menaikkan modal hutang diperlukan kepada pelaburan pasti dana merancang daripada bank-bank yang strategi kemasukan kewangan menarik lebih banyak deposit. Pembuat polisi sepatutnya menggubal dasar yang mempromosikan pembangunan pasaran kewangan kerana dasar sedemikian akan melengkapkan strategi kemasukan kewangan dan firma bank akan mempunyai lebih akses kepada modal hutang. Akhir sekali, pengurus-pengurus kewangan perlu mencari jalan untuk akses kewangan dan serentak memaksimumkan faedah-faedah penghadang cukai hutang dalam struktur modal mereka prestasi firma peningkatan itu.

Kajian menyumbang kepada kesusasteraan dalam dua cara utama. Pertama sekali, tidak seperti kajian sebelum yang guna pelbagai pembolehubah dimensi menentukan struktur modal seperti firma khusus dan negara pemboleh ubah tertentu; kajian menunjukkan ini menggunakan pembolehubah kemasukan kewangan sebagai penentu struktur modal. Kedua, kajian seterusnya meneroka kesan sebagai orang tengah pembangunan kewangan di hubungan antara rangkuman kewangan dan hutang; serta bersederhana kesan rangkuman kewangan di hubungan antara struktur modal dan prestasi firma, yang telah tidak diendahkan dalam kesusasteraan struktur modal.

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This thesis submitted to the Senate of Universiti Putra Malaysia has been accepted as fulfillment of the requirements for the degree of Doctor of Philosophy. The members of the Supervisory Committee are as follows:

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LIST OF ABBREVIATIONS

ATM	Automated Teller Machine per 100,000 adult
BB	Bank Branch per 100,000 adult
BCPS	Ratio of Bank Credit to Private Sector
BTP	Ratio of Book Value of Equity to Market Value of Equity
FA	Ratio of Property, Plant, and Equipment to Total Assets
GDPG	Gross Domestic Product Growth
GMM	Generalised Methods of Moment
INF	Inflation Rate
INT	Interest rate
MCGDP	Ratio of Market Capitalisation to Gross Domestic Product
MTB	Ratio of Market Value of Assets to Book Value of Assets
NDTS	Ratio of Non-Debt Tax Shield to Total Assets
PRFTS	Ratio of Earnings before Interest and Tax to Total Assets
SLlog	Log of Size
TAX	Ratio of Tax Liability to Taxable Income
Tobin's Q	Ratio of Market Value Equity plus Book Value of Debt to Book Value of Total Assets

CHAPTER 1

INTRODUCTION

1.1 Background of the Study

Capital structure is a component of the financial structure and it denotes the ratio of the various long-term sources of financing. The capital structure of firms comprises debt and equity securities use to finance their assets. Equity comes into effect when firms sell parts of their ownership rights to raise capital. Debt is a contractual agreement, which allows firms to borrow money and make repayment with interest for a specific period of time (Ross et al., 2017). Debt and equity have different cost to the firms, and the main issue in the capital structure literature is to determine the appropriate amount of debt and equity needed to finance the operation of firms. The determination of the appropriate amount of debt and equity finance remains an unresolved issue (Dao & Ta, 2020). Firms' focus more on the debt component of capital structure because it is a double edge sword that can increase firm-value performance when the economy is performing well but debt can decrease firm performance when the economy is performing poorly. Additionally, debt needs payments of fixed interest and too much debt increases the firms' inability to repay amount borrowed and fixed interest, particularly when the economy is performing poorly (Ross et al., 2017). Although debt increases financial risk, most firms around the world may use more debt because of the debt interest tax-shield which could increase firm-value performance.

Fundamentally, financial development is about overcoming costs incurred in the financial system. The process of reducing the costs of obtaining information, enforcing contracts, and making transactions resulted in the emergence of financial contracts, markets, and intermediaries. The five main functions of a financial system are to produce information ex ante about possible investments and allocate capital, monitor investments and exert corporate governance after financing is provided; facilitating the trading and management of risk, mobilize and pool savings; and to ease the exchange of goods and services. Financial development therefore occurs when financial markets, instruments, and intermediaries ease the effects of transactions costs, information, and enforcement; thus do a better job to provide the major functions of the financial sector in an economy (World Bank Report, 2016). But, financial development level is low in several developing countries. Specifically, the cost of financial intermediation, mobilizing and pooling savings and transaction costs are high, which is an indication of inefficiency and underdevelopment of the financial sector (Ezeibekwe, 2020). In a country with weak financial development, firms may have difficulty to obtain debt capital needed to finance profitable investments, and capitalize on the debt interest tax-shield to maximize firm performance.

As financial development level improves and financial inclusion efforts further makes more deposits available to banks, firms may have easy access to debt capital. Finance is a prominent factor, which boosts the foundation of economic growth and development (Goel & Sharma, 2017). Financial constraints affect firms from rich and poor economies and are an active area of corporate finance research. Research had specifically shown that lack of access to finance is a first-order constraint to innovation, growth, and development (Ayyagari et al., 2008; 2011) and that some businesses are negatively affected by financial and institutional inclusive growth (Beck et al., 2005; 2006). Much empirical evidence is convinced that an effective, efficient, and well-functioning financial system are crucial to channel funds to the most appropriate productive uses and allocate it to where it is needed the best, and ultimately boost economic growth, increase business opportunities and income distribution. Financial inclusion (access to finance) and available inclusive financial services are relevant to economies of growth and development (Demirguc-Kunt et al., 2018; De la Torre et al., 2017). Therefore, better financial accessibility is the initiative to create financial services such as credit, savings, payment, insurance, and other risk-bearing management product available and affordable to facilitate sustained productivity and growth, especially for households and firms who play a crucial role in uplifting the economy to a greater height (Ahamed et al., 2017).

Therefore financial inclusion (i.e. access to formal financial services) has the potential to help transform the lives of low-income households and businesses of firms. The access and usage of saving, transaction, and credit services can play a central role in household efforts to smooth consumption, firms to invest in human or productive capital, and reduce exposure to uncertainties. These services are, specifically important for the poor in developing countries. Besides, it also helps those who face fluctuating incomes in the informal sectors, and who are vulnerable to significant health and institutional shocks (Demirguc-Kunt, et al. 2019). About 2.5 billion people are excluded from financial services globally, specifically those impoverished who live in middle-income countries and the poorest parts of the world. It is also estimated that approximately 80 percent (300 million people) of the population from 11 Sub-Saharan African Countries, do not have a formal bank account, and as a result, they are deemed 'financially excluded'. These conditions indicate the importance of financial inclusion in developing countries. Moreover, the fundamental barrier to slow development in developing countries especially African is attributed to lack of money (Zins & Weill, 2016).

Furthermore, about 515 million adults acquired a financial account over three years whereas 1.2 billion people had opened an account with a formal financial institution or provider of mobile financial services between 2010 and 2017. By any metric, this is a remarkable improvement, but so much remains to be done. By 2017, 1.7 billion people aged 16 and above had zero access to an account, which is about 31 percent of the world's adult population (Demirguc-Kunt et al., 2018). Moreover, the report showed that every one out of two people in the world did not have access to a formal savings account, insurance, loan, and other financial services. The report also showed that less than a quarter of adults possessed an account, in the formal financial institution and most of them used informal methods to save, and their borrowings were mainly for family, friends, and other traditional techniques (Demirguc-Kunt et al., 2018). According to Deep Knowledge Analytics & Future Fintech (2019), the figure of adults excluded from financial services in many economies is greater than the adult population living below the poverty line of $2 per day. A study on financial inclusion in terms of ownership and use of accounts showed that financial exclusion among individuals resulted from high minimum balance to maintain a bank account, non-close proximity to financial institutions, lack legal rights, and not environmentally sustainable (Allen et al., 2016).

The money banking sector is leading the African continent, especially East Africa where more than 70 percent of Kenyans are mobile money customers. In sub-Saharan Africa, 36 out of the 54 countries have mobile banking services. Yet 2.5 billion adults in lower and middle-income nations do not have access to banking services (Zins & Weill, 2016). Moreover, saving habits in the continent of Africa differ in comparison with the world. The major money-saving motivation in Africa includes education (21.3 %) and farming (19.6 %) whereas for individuals worldwide it is 23.9 percent.
The savings motivation factor in Africa are shown below:

Table 1.1: Saving motivation factors in African countries

Savings motivation in Africa	Percentages
Education	21.3%
Farming	19.6%
Retirement (savings for old age)	23.9%

[Source: Zins & Weill (2016) sourced (Demirguc-kunt et al., 2015)]

Furthermore, 37 percent of the major source of credit in Africa consists of family and friends, followed by 7.9 percent from stores, 6.7 percent borrowed formally, and finally 4.7 percent borrowed from private lenders. In Africa, 41 percent of its individuals were reported borrowing from informal sources, and about 51.4 percent of the individuals are borrowed from any source in the past one year, a figure higher than 42.4 percent globally (Zins & Weill, 2016). Therefore, the source of the major savings in Africa was shown below:

Table 1.2: Major credit sources in African countries

Credit Sources	Percentages
Family and Friends	37.5%
Store	7.9%
Formal Borrowing	6.7%
Borrowing from other private lenders	4.7%
Borrowing from informal sources	41%
Borrowing from every source	51.4%

[Source: Zins & Weill (2016) sourced (Demirguc-kunt et al., 2015)]

A study conducted in Africa (United Nations Development Programme, 2015) revealed that the country with the highest rate of financial inclusion in Africa is Kenya with 67 percent, Nigeria with 60 percent, and Cameroun 47 percent. While other countries in

Africa had less than 30 percent rate of financial inclusion, and Mozambique had 13 percent with the lowest rate. Hence, Table 1.3 shows financial inclusion in some African countries.

Table 1.3: The rate of financial inclusion in some African countries

Countries	Percentages
Kenya	67%
Nigeria	60%
Cameroun	47%
Uganda	28%
Zambia	23%
Senegal	20%
Benin	20%
Mozambique	13%

[Source: Demirguc-kunt et al. (2015) sourced (Global Findex data 2014, World Bank)]

Table 1.4 illustrates the penetration of accounts in Africa based on regions. South Africa, has the highest percentage in Africa in terms of account penetration with 42 percent, followed by West Africa with 23 percent, East Africa with 22 percent, North Africa 20 percent, and lastly Central Africa with 7 percent. Despite the progress of financial inclusion globally, Africa is still left behind. Therefore, the variations in the account penetration sample showed uneven progress within the continent, which may be a reason for massive unemployment and abject poverty that crippled the continent.

Table 1.4: Regional account penetration in Africa

AFRICA	PERCENTAGES
Southern Africa	42%
Western Africa	23%
Eastern Africa	22%
North Africa	20%
Central Africa	7%

[Source: Demirgüç-Kunt & Klapper (2013) (Authors' calculations using Global Findex data)]

However, in Asia issues related to inequality are growing rapidly. Inequality had increased the economies of the Asian nations, which collectively account for more than 80 percent of the region's population (Mylenko & Park, 2015). This growing inequality encompassed income and development levels, throughout Asia. Hence, the financial inclusion growth, which spread investment opportunities and the proceeds of growth evenly across the entire region had emerged as a top strategic policy in Asia despite the growing concerns over inequality. Moreover, financial inclusion growth is an inclusive financial system that expands financial access to products and services to the poor and vulnerable individuals, households, and firms. Access to finance is a strategic policy in Asia, which intends to protect the poor against negative shocks and balance their consumption and ultimately expand their welfare. It is also intended to improve their human capital and opportunities productively. Besides, the importance of growing awareness of financial inclusion in Asia, encouraged financial regulators from more than 20 nations made commitments on financial inclusion under the Maya Declaration in 2011 to create a sound and enabling environment, which included the use of modern technology to increase access to finance and also lower cost of financial products and services; to create a sound regulatory framework that balances financial inclusion, integrity, and stability; to create consumer protection and integrate it with empowerment as a pillar for inclusive growth; to create the use of data to find solutions and formulate proper policies (Mylenko & Park, 2015).

In Asia, it is estimated that 1.3 million adults, or 46 percent of the adults had accounts in formal financial institutions. The figure is higher than that of Latin America at 39 percent but lowers to that of the high-income nations at above 90 percent. In China, Singapore, Malaysia, Thailand, Korean Republic, Mongolia, and Sri Lanka, the majority of adults have formal bank accounts, yet 17 out of 26 nations had less than 40 percent accounts (Mylenko & Park, 2015). Therefore, listed below is a share of the adult population with a formal financial institution account in Asia.

Table 1.5 shows the account penetration in South East Asia, where Singapore has 98 percent of the highest account penetration in South East Asia, followed by Thailand with 73 percent, and Malaysia with 67 percent. Cambodia is the South East Asia country with the lowest account penetration with 4 percent, Indonesia with 20 percent, Vietnam with 21 percent, the Philippines with 26 percent, and Lao PDR with 27 percent.

Account penetration in Asia sub-regions.

Table 1.5: Account penetration in South East Asia

Countries	Percentages
Singapore	98%
Thailand	73%
Malaysia	67%
Lao PDR	27%
Philippines	26%
Vietnam	21%
Indonesia	20%
Cambodia	4%

[**Source:** Mylenko & Park (2015) sourced (Demirguc-kunt & Klapper, 2013)]

Table 1.6 shows the account penetration in South Asia, where Sri Lanka is the country with 69 percent which is the highest percentage in terms of account penetration in South Asia, followed by Bangladesh with 40 percent then subsequently Malaysia had 35 percent with the third-highest. Afghanistan is the South Asia country with the lowest account penetration with 9 percent, followed by Pakistan with 10 percent, and then Nepal with 25 percent.

Table 1.6: Account penetration in South Asia

Countries	Percentages
Sri Lanka	69%
Bangladesh	40%
India	35%
Nepal	25%
Pakistan	10%
Afghanistan	9%

[**Source:** Mylenko & Park (2015) sourced (Demirguc-kunt & Klapper, 2013)]

Although there were improvements in the financial inclusion levels in Latin America between 2011 and 2014, Latin American countries like Brazil, Costa Rica, and Jamaica scored a high index of financial inclusion. This is because these countries financial service providers had financial strategies that increased inclusive growth. For instance, in Brazil, high levels of financial inclusion were achieved through the growth and stability of the economy, coupled with the fact that the policies improved distribution channels, promoted transparency, fostered financial literary, and designed financial services regulation to suit the poor and the vulnerable in the economy. By 2014, many other nations in Latin America joined the ranks of better than average performers like Chile, Uruguay, and Venezuela. This is because these countries' financial inclusion index improved due to the increase in mobile financial services, which increased the growth rapidly. In Chile, for instance, a high degree of access to financial services is achieved through efforts aimed at fulfilling the commitments made under the 2011 Maya Declaration (Dabla-Norris et al., 2015).

Moreover, between 2011 and 2013 the number of ATMs and bank branches per 100,000 adults witnessed significant growth. In 2011 the number of ATMs per 100,000 adults was 40 percent whereas the number of bank branches per 100,000 adults was 24 percent and the overall percentage of ATMs and bank branches for that same year were 64 percent. Additionally, in 2013, the number of ATMs per 100,000 adults was 55 percent whereas the number of bank branches per 100,000 adults was 33 percent, and the overall percentage of ATMs and bank branches for that same year was 78 percent (Rojas-Suarez, 2016).

The ATMs depicted a 40 percent penetration rate whereas the Bank Branches exhibited a total of 24 percent penetration rate in 2011. On the other hand, in 2013 the percentages rose to 45 percent for ATMs and 33 percent for Bank Branches. Therefore, the combined percentages for both the penetration of ATMs and Bank Branches in Latin America were 64 percent for 2011 and 78 percent for 2013, respectively. Table 1.7 shows the ATM's and Bank Branches' penetration in Latin America.

Table 1.7: ATMs and Bank Branches Penetration in Latin America

Year	ATMs	Bank Branches
2011	40%	24%
2013	45%	33%

[Source: Rojas-Suarez (2016) (Global findex data 2014, World Bank)]

Based on Table 1.8, 34 percent of the adults had accounts in sub-Saharan Africa in comparison to other regions in the world. On the other hand, 14 percent of adults from the Middle East was the only region Africa had exceeded in terms of account penetration. This resulted from religious belief, interest rate given by the banks, the cost of maintaining the account, or other attributes associated with being formally financially inclusive. The high-income countries had the highest percentage (94%) of account penetration because digital financial services and mobile money banking are at their peak. East and pacific Asia had 69 percent, which was next to the high-income countries, and stratified ways to which they will ease account opening and access to finance to its citizens. Moreover, 51 percent of adults who have accounts both in Europe and Central Asia, Latin America, and the Caribbean are progressively embracing the digital financial service and mobile money banking within these regions. However, there are miles to go when compared to high-income countries (Demirguc-kunt, 2015).

Table 1.8: Global Account Penetration

Regions	Percentages
High income	94%
East Asia and pacific	69%
Europe and Central Asia	51%
Latin America and the Caribbean	51%
South Asia	46%
Sub Saharan Africa	34%
Middle East	14%

[Source: Demirguc-kunt et al., (2015) (Global findex data 2014, World Bank)]

Globally, it is observed that almost all adults have accounts, but only 60 percent of them have bank accounts. Those, who have both bank accounts and mobile money accounts make up 1 percent of society. In Africa, one-third of account holders or 12 percent of adults who have accounts are observed to have mobile money accounts. Therefore, the report further showed that within the 12 percent, 6 percent had both mobile and bank accounts whereas the other 6 percent had mobile accounts only. In East Africa, 20 percent of adults embrace money mobile accounts whereas only 10 percent have mobile money banking. Moreover, the disparity of figures in the sub-regions makes Kenya the highest number of adults (58%) with mobile money accounts, followed by Somalia, Tanzania then Uganda with 35 percent. The number of adults with accounts in South Africa was also high with14 percent, whereas only 2 percent had a mobile money account.

Financial inclusion is also measured globally based on the Automated Teller Machines (ATMs), the number of bank branches, and the number of account holders (Ayyagari & Beck, 2015; Elsayed & Elatroush, 2019). The penetration of automated teller machines (ATMs) and commercial bank branches (BB) per 100, 000 adults varied globally. Automated teller machines (ATMs) and commercial bank branches (BB) per 100,000 adults of global penetration had left developing countries far behind. The Sub Saharan African countries (SSA), have the lowest percentage number of ATM's and BB penetration. The region has over 40 countries but ATMs and BB penetration are 7.0 and

4.1 percent, respectively. The rate of penetration stood at 17.7 percent for ATM's and 10.6 percent for BB in a developing Asia. On the other hand, the penetration rate for ATMs was 22.0 and 19.1 for BB in the Middle East and North Africa. The highest ATM's and BB penetration is recorded in the high-income countries with ATM's 76.8 and BB at 32.3 percent, followed by Europe whose ATM's and BB penetration stood at 51.6 and 23.3 percent and then Latin America and the Caribbean with ATM's 37.3 percent and BB 17.3 percent, respectively. Table 1.9 shows the global penetration of ATMs and Bank Branches per 100,000 adults (Ayyagari & Beck, 2015).

Table 1.9: Global Penetration of ATMs and Bank Branches per 100,000 adult

Regions	ATM'S	Bank Branches
High income	76.8%	32.3%
Europe	51.6%	23.3%
LAC	37.3%	17.3%
MENA	22.0%	19.1%
Asia	17.7 %	10.6%
SSA	7.0%	4.1%

[Source: Ayyagari & Beck (2015) : (Demirgüç-Kunt and Klapper, 2013)]

Table 1.10 shows a summary of the world's unbanked adult population. South Asia is the world sub-region and has the highest population of unbanked adults (31 percent), followed by East and Pacific Asia with 24 percent, then Africa with 17 percent. The world sub-region with the lowest population of adults unbanked is the high-income countries with 3%, followed by the Middle East and other economies with 4% each, then subsequently 5 percent for Europe and Central Asia and 10 percent for Latin America and the Caribbean, respectively.

Table 1.10: World's unbanked adults by region Adults without an account (%), 2014

Regions	Percentages
High Income	3%
Middle East	4%
Europe and Central Asia	5%
Latin America and the Caribbean	10%
Sub Saharan Africa	17%
East Asia and Pacific	24%
South Asia	31%
Other Economies	4%

[Source: Demirguc-kunt et al. (2015) (Global Findex data 2014, World Bank)]

With these statistical figures it is seen that in terms of access to finance globally, developing countries are backward. Hence, the present study emphasized the focus on developing countries. However, all the facts stated above, on how developing countries are left behind in terms of financial inclusion, one can say that research based on financial inclusion in developing countries would never cease to exist because there are so many developing countries in the world, specifically Africa a nation far behind in terms of financial inclusion. Therefore, the present research is crucial to exhibit the problems and suggest solutions via empirical study and policy.

1.2 Statement of Problem

Financial inclusion and capital structure

It is estimated that 2.5 billion people are excluded from financial services globally, also estimated that approximately 80 percent (300 million people) of the population of 11 Sub-Saharan African Countries, do not have a formal bank account, and as a result they are deemed financially excluded. In Asia, it is estimated that 1.3 million adults, or 46 percent of the population consisting of adults having accounts in formal financial institutions. The figure is higher than that of the Latin America at 39 percent but lower to that of the high income nations at above 90 percent.

A study on financial inclusion in terms of ownership and use of accounts shows that, the main reason for being financially excluded among individuals is high minimum balance to maintain bank account, non-close proximity to financial institutions, lack legal rights, and not environmentally sustainable (Allen, Demirguc-Kunt, Klapper, & Martinez Peria, 2016). All these reasons partly explain why banks deposit base are lower than expected, and some firms have difficulty raising money from banks.

Furthermore, most firms in developing countries have inadequate access to debt capital needed to finance profitable investment opportunities (Fowowe, 2017). Moreover, the debt-to-total assets ratio of firms in most developing countries appear lower compared to the developed countries, which may be partly caused by the banks inability to attract sufficient deposits to lend to firms. But, financial inclusion that increases access to finance may play an important role in increasing debt level in the capital structure of firms in developing countries (Wasiuzzaman & Nurdin, 2019).

Financial development moderating the relationship between financial inclusion and Capital structure

Over the years the level of financial development is improving in some developing countries as efforts are being made to reduce transaction costs and improve the financial intermediation function. However, the level of financial development in most developing countries is lower compared to the developed countries. Moreover, the financial sector in developing countries is still characterized by high transaction costs and inefficiency when allocating financial resources to the deficit sectors such as firms (Ezeibekwe, 2020).

In spite the fact that financial market development can complement financial inclusion (access to finance) via increasing firm's access to debt capital, yet the moderating impact of financial development on the link between financial inclusion (access to finance) and capital structure (debt) of firms in developing countries remain unexplored. Furthermore, financial market development (especially debt market development) reduces costs of borrowing and makes it easier for firms to raise debt capital (Khémiri & Noubbigh, 2018). But debt market development is still at the developmental stage in most developing countries indicatng that the problem of access to debt capital may persist. However, as the development of the debt market improves, financial inclusion (access to finance) may increase as banks can increase their deposit base, making firms have more access to raise debt capital to the desired level.

Financial inclusion moderating the relationship between capital structure and firm performance

Firm performance has been adversely affected in most developing countries. One of the reasons for the declining firm performance is that several firms have inadequate access to debt capital (IMF Report, 2019) needed to finance profitable investments and maximize the tax-shield benefit of debt to increase firm performance. Despite the fact that financial inclusion can enable firms have more access to debt capital needed to maximize the interest tax shield benefits of debt to increase firm performance, yet the impact of financial inclusion (access to finance) on the relationship between capital structure (debt) and firm performance in developing countries is unexplored by researchers and practitioners. Although, the debt-to-total assets ratio of firms in most developing countries are generally low, financial inclusion (access to finance) may resolve this sub-optimal debt problem caused by lack of firms' access to debt capital. Moreover, the debt-to-total assets ratio of firms in most developing countries are generally lower compared to the developed countries, which may be partly caused by some banks inability to attract sufficient deposits to lend to firms. But, as financial inclusion (access to finance) enhances the banks deposit base because more depositors bank their money, firms can have more access to debt capital needed to maximize the debt interest tax-shield and increase firm performance.

1.3 Research Hypothesis

The research is determined to provide in due course empirical answers to the following research hypothesis. Each hypothesis has two models specification, this is because the financial inclusion (automatic teller machine (ATM) and bank branches (BB)) proxies are two and each proxy is tested, to have a better and robust result for financial inclusion.

a) There is no positive relationship between capital structure and financial inclusion.

b) Financial development does not positively moderate the relationship between financial inclusion and capital structure.
c) Financial inclusion does not moderate the relationship between capital structure and firm performance.

1.4 Research Objectives

The broad research objectives investigated the relationship between financial inclusion, capital structure, financial development, and firm performance via data from developing countries. The specific objectives included:

a) To examine the effect of financial inclusion on capital structure (debt ratio).
b) To investigate the moderating effect of financial development on the relationship between financial inclusion and capital structure (debt ratio)
c) To examine the moderating effect of financial inclusion on the relationship between capital structure (debt ratio) and firm performance.

1.5 Motivation of Study

Issues related to financial inclusion and capital structure are widely debated in the economic and finance literature. (Demirguc-Kunt, et al. (2018) stated that every one out of two people in the world does not have access to a formal savings account, insurance, loan, and other financial services for financial inclusion. On the other hand, Khémiri & Noubbigh (2018) stated that capital structure choice is a puzzle, and it remains a puzzle to date. Furthermore, researchers ignored the importance of modeling financial inclusion and capital structure alongside financial development and firm performance in developing countries. The idea of providing an inclusive financial system was not only aimed at integrating numerous excluding the poor into the formal financial system but also challenged challenges the mainstream financial institution to reach the unbanked portion of the economy (Beck et al., 2015)

1.6 Significance of the Study

The present study focused on the link between financial inclusion and capital structure. Moreover, the study explored the moderating role of financial inclusion between capital structure (debt) and firms' performance. Additionally, the study investigated the moderating role of financial development between financial inclusion and capital structure. Hence, the study integrated the financial inclusion theory with M-M and tradeoff theories to explain the relationship between capital structure, financial inclusion, financial development, and firm performance. Hence, firm managers could have more financial inclusion (access to debt capital) and take advantage of the debt interest tax shield to increase firm performance as financial inclusion improved. Policymakers were encouraged to further strengthen financial inclusion and financial development policies to reduce barriers to external capital and enable firms the accessibility to debt capital.

1.7 Outline of Study

The study was divided into five chapters. Chapter one delineated the background of the study on financial inclusion, capital structure, financial development, and firm performance. Chapter two presented the relevant financial inclusion theory, theoretical framework, and capital structure theories review, review of empirical evidence on financial inclusion, capital structure, financial development, and firm performance in developing countries. Next, Chapter three discussed the data, model specification, estimation method, and justification of variables. Chapter four presented the analysis and discussion of results. Finally, Chapter five summarized and concluded the study.

1.8 Summary

The section highlighted the background of the study stressing the importance of financial inclusion, capital structure, financial development, and firm-value performance in developing countries. The section also states the issue for which the research is being conducted. The hypothesis and objectives of the study are coined in line with the issues the research intended to answer. Moreover, the section also shows the motivation and significance of the study. Lastly, it states how the research is been organized.

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