The Relationship between capital structure, free cash flow, diversification and firm performance

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ABSTRACT

This study investigated whether there are inter-relationships among capital structure (financial leverage), free cash flow, diversification and firm performance. To this, 78 active firms in this area were selected between 2011 and 2015. Internal independent variables involve capital structure, free cash flow, diversification and firm performance. To study inter-relationships of variables, simultaneous equation system and STATA software were applied. Results indicated that a positively significant relation exists between free cash flow and firm performance in 95% level of significance. There is a negatively significant correlation between capital structure and free cash flow in 95% level of significance. Between free cash flow and diversification, a negative and significant relation exists, with 90% level of significance. And, a bi-directional relation exists between capital structure and firm performance in 90% level of significance. There is no bi-directional relation between diversification and firm performance. Finally, according to results, capital structure and diversification have no bi-directional relation.

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Peer review under responsibility of **UCT Journal of Management and Accounting Studies**