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The Impact of Macroeconomic and Institutional Factors on Corporate Financial Flexibility with the Moderating Impact of Corporate Governance: Evidence from Sri Lanka

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Abstract

Corporate financial flexibility is a key determinant of corporate financial policies and cash positions of business organizations. Therefore, it has become a part of business strategy. Corporate financial flexibility shows the ability of businesses to raise capital at a low cost to invest easily and quickly in value-enhancing projects and to meet an unexpected increase in working capital requirements. Although many studies have tested the impact of institutional and macroeconomic factors on corporate financial flexibility, corporate governance as a moderating variable between corporate financial flexibility and institutional and macroeconomic factors has not been well established. Hence, this paper evaluates the impact of institutional and macroeconomic factors on corporate financial flexibility by employing corporate governance as a moderating variable. The sample consists of 174 companies listed on Colombo Stock Exchange for seven years, starting from 2014 to 2020. The results show that firm profitability, GDP growth, and banking sector development have a significant impact on corporate financial flexibility. Further, corporate governance moderates the relation between profitability and financial flexibility. Findings are useful for corporate decision-makers for effective management of corporate financial flexibility and to obtain maximum benefits from available funds. As a pioneer study that identifies the moderating impact of corporate governance on the relation between institutional and macroeconomic factors and corporate financial flexibility, this study makes a novel contribution to the existing knowledge in the field of corporate finance.

Keywords: *Corporate financial flexibility, Corporate governance, Institutional factors, Macroeconomics factors, Sri Lanka*