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Target behavior and lumpy investments

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Abstract

This study presents an empirical investigation whether lumpy investment behaviors by firms affect their readjustment toward target leverage ratios. Using a data sample of Japanese listed firms from 1978–2008, it is found that firm investment spikes have a larger effect on debt than equity issuances. The positive effects vary with firms' debt positions: firms with below-target debt are more (less) likely to issue debt (equity) compared with those with above-target debt. It is also found that financially constrained firms, with above-target debt, are more responsive to investment spikes than their financially unconstrained counterparts.

Keywords: Capital structure, information asymmetry