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Information Availability, Information
Quality and the Financial Structure of
Belgian SMEs

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Information Availability, Information Quality and the Financial Structure of Belgian SMEs

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Abstract

In this paper we test whether the amount and/or quality of financial statement information affect the financial structure of Small and Medium Enterprises (SMEs). We explore this issue for Belgian SMEs because there are important differences in disclosure and audit requirements among them. Consistent with the traditional view that asymmetric or incomplete information restricts access to external funds, our results indicate that both the amount and the quality of financial statement information are positively related to SME leverage. In addition, we find that leverage is positively related to asset structure, growth (prospects) and median industry leverage; and negatively related to firm age and profitability.

KEY WORDS: financial structure, leverage, SME, information asymmetry, financial statements, external audit

JEL CLASSIFICATION: G32, M41, M42

1. INTRODUCTION

Entrepreneurs can finance their firms through equity or debt. Seminal work by Modigliani and Miller (1958) demonstrates that in a 'perfect' world the choice between equity and debt is irrelevant. When taxes and other market imperfections are introduced, there will be a single optimal financial structure because firms will increase debt financing until the advantage of tax deductibility of interest expenses is counterbalanced by the disadvantages of other market imperfections like bankruptcy costs (i.e., *Trade-Off Theory*). Other theories have challenged this view (see, Harris and Raviv (1993) for an overview). One of the main alternative theories is *Pecking-Order Theory* that predicts that due to asymmetric information firms will prefer internally generated funds over debt, which in turn, is preferred over equity financing (Myers 1984; Myers and Majluf 1984).

While empirical research originally focused on the financial structure choice of large/listed firms, the economic importance of SMEs (see e.g., Psillaki and Daskalakis 2008) has fuelled research on SME financing. SMEs do not only account for 99% of all European firms, they are also responsible for approximately two-thirds of total turnover and employment (European Observatory for SMEs 2000).

In addition, previous results for large/listed firms need not apply to SMEs. Firstly, the fiscal advantages of debt will typically be more limited for SMEs, because (i) SMEs have a higher cost of debt than large firms (see e.g., Holmes et al. 1994), given that banks consider SMEs to be more risky than large firms (see e.g., Scherr et al. 1993); (ii) small firms have, on average, lower profit margins because they operate in less concentrated and more competitive markets; and (iii) SMEs are typically subject to lower tax rates (see e.g., McConnell and Pettit 1984; Pettit and Singer 1985). Secondly, financial structure decisions in SMEs are often inspired by the entrepreneur's desire to maintain family control over the firm (see e.g., Ang 1992). Finally, information asymmetry problems are found to be more severe for SMEs (cf. Section 2).

We add to the growing body of research on SME financial structure by formally testing the impact of both quantity and quality of publicly available information using a very broad sample of Belgian SMEs. It is generally accepted that informational opacity hinders SMEs access to external funds (see e.g. Berger and Udell 1998), but the effect of differences in (quality of) publicly available information has been barely examined.

In line with the traditional information asymmetry argument, our results indicate that both the amount and the quality of publicly available information are positively related to SME leverage. More specifically, we observe a significantly positive relationship between the level of FS detail and leverage; and a significantly positive relationship between FS quality and leverage. Findings for the other firm-specific variables included in our model are generally consistent with prior studies: SME leverage is positively related to asset structure, growth (prospects) and median industry leverage; and negatively related to firm age and profitability. Results for firm size are inconclusive.

The paper proceeds as follows. In Section 2, we briefly review the main financial structure theories and formulate our hypotheses. Our sample and variable selection are described in Section 3. In Section 4, we present the methodology and our empirical results. We conclude in Section 5.

2. THEORETICAL REVIEW AND FORMULATION OF HYPOTHESES

Pecking-Order Theory (henceforth POT), as proposed by Myers (1984) and Myers and Majluf (1984), is built around the fact that inside management is better informed of the true value of the firm than outside investors. Managers will prefer those sources of funds that are least susceptible to undervaluation resulting from information asymmetries. Based on this premise, firms will first opt for internally generated funds (inside equity), then for debt and only as a last resort for outside equity. Under this theory, a firm's financial structure is the outcome of previous independent decisions and there is no 'optimal' ratio of debt to equity (Cole 2008). Many empirical studies support the appropriateness of POT in explaining the financing of SMEs (see e.g., Norton 1990; Lopez-Gracia and Aybar-Arias 2000; Ou and Haynes 2006).

In contrast to POT, *Trade-Off Theory* (henceforth TOT) predicts an optimal ratio of debt to equity, where the advantages of debt are carefully balanced against the disadvantages (see e.g., Brennan and Schwartz 1978; DeAngelo and Masulis 1980, Bradley et al. 1984). The main advantage of debt relates to the fact that interests, as opposed to dividends, are deductible for fiscal purposes (Modigliani and Miller 1963; DeAngelo and Masulis 1980). However, a higher debt ratio leads to higher costs of financial distress (Kraus and Litzenberger 1973; Kim 1978) and possible

agency problems between the shareholders and its financial creditors (e.g., the risk of underinvestment and/or asset substitution) (Jensen and Meckling 1976).

Whereas some studies have explicitly tried to distinguish between these theories (see e.g., Lopez-Gracia and Sogorb-Mira 2008), it appears that all aforementioned theories help to explain SME financial structures. Similar conclusions are drawn based on survey studies. Graham and Harvey (2001), for example, find that more than eighty percent of the respondents indicated that a target leverage ratio guided their decisions (which is consistent with TOT), while they also indicated a preference to first using retained earnings for financing purposes (which is consistent with POT). In a similar vein, Myers (2001) argues that while the different theories based on information, taxes and agency costs are relevant for financing choices, “[t]here is no universal theory of the debt-equity choice, and no reason to expect one” (Myers 2001:81). Moreover, because competing theories often yield the same prediction, a statistical finding is often consistent with two or more financial structure theories (Myers 2001).

Based on the aforementioned theories, we derive predictions regarding the determinants of SME financial structure. Firstly, the lack of publicly available information about SMEs (and the resulting information asymmetry) is considered to have an important impact on their financial structure. It is typically argued that asymmetric information problems are far more severe in SMEs relative to large firms because of the lack of publicly available, uniform and detailed accounting information. Moreover, the quality of their FS is assumed to vary because they are typically not audited (Pettit and Singer 1985; Orteiz-Molina and Penas 2006). As a result, Berger and Udell (1998: 616) refer to “acutely informationally opaque” small businesses. The inability of lenders and/or investors to distinguish between high- and low-quality firms because of incomplete information is likely to raise the firm’s cost of funding. As a result, small firms may actually be inhibited from using external funds because they cannot bear the related costs (Weinberg 1994). Despite the importance of the issue, to our knowledge, no prior studies have explicitly tested the impact of information availability and quality on SME financial structure. Gregory et al. (2005) provide a notable exception as they include a dummy variable related to information availability in their model of SME financial structure. Nevertheless, this dummy variable is a rather crude information proxy.¹

¹ The information proxy in Gregory et al. (2005) is based on a survey and takes a value of one if the company indicates that records on all aspects of the business (including “the firm’s income sheets,

The Belgian environment provides an interesting setting to study the impact of differences in (quality of) information on the financial structure of SMEs. Firstly, Belgian firms are required to file their FS according to a prescribed format in which the different items to be disclosed are explicitly defined. There are two FS formats, being a complete format and an abbreviated format. The latter is less detailed and has lower information value than the former. A firm has to file the complete format if it has more than 100 employees, or if at least two of the following criteria are satisfied: (i) at least 50 employees (yearly average); (ii) turnover (excluding VAT) of at least 7300000 EUR; and/or (iii) total assets of at least 3650000 EUR. Firms that do not meet the aforementioned criteria are allowed to prepare their FS according to the abbreviated format. Importantly, all aforementioned criteria fall below those used in the European Commission SME definition (cf. Section 3.1 for more details). Accordingly, certain Belgian SMEs disclose the complete format of the FS (and provide the same amount of information as large Belgian firms) and other Belgian SMEs file the abbreviated format of the FS (and therefore provide less information). Thus, based on the format of the FS filed, we are able to test the impact of information quantity on SME financial structure. Secondly, the aforementioned size criteria also determine whether the firm is subject to a mandatory external FS audit. Firms that fall below these size criteria can opt for a voluntary external FS audit. Given that the accuracy of the FS is verified during an audit, we use a FS audit as a signal about FS quality (and hence quality of the publicly available information). We therefore predict a positive relationship between leverage and both the amount and the quality of information:

H1: More detailed FS are positively related to leverage.

H2: Audited FS are positively related to leverage.

Following both TOT and POT, studies on the financial structure of SMEs typically control for firm size. Larger firms that tend to be more diversified, have lower probabilities of default than smaller firms (see e.g., Warner 1977; Ang et al. 1982; Pettit and Singer 1985). In other words, larger firms have lower bankruptcy costs

expense sheets, and balance sheets, tax records, tax statements, tax worksheets, and all other pertinent records") are available and zero otherwise.

and based on TOT a positive relation between leverage and firm size is therefore expected. Moreover, because more information is typically available for larger firms than small firms, the former will have less information asymmetries (see e.g., Cole 2008; Psilakis and Daskalakis 2008). Based on POT, a positive relation between leverage and firm size is therefore predicted. Whereas both theories predict a positive relationship between firm size and leverage, empirical findings are ambiguous: both positive (see e.g., Michaelas et al. 1999; Sogorb-Mira 2005), and negative relationships (see e.g., Esperança 2003; Heyman et al. 2008) are documented. Based on Belgian data, Heyman et al. (2008) report a significantly negative relation between leverage and firm size. Given our focus on Belgian firms, we hypothesize that:

H3: Firm size is negatively related to leverage.

Information asymmetries are assumed to be less severe for older firms than for younger firms, because the former have established a track record and reputation (e.g., regarding their ability to meet (financial) obligations in a timely manner) (Ang 1991; Diamond 1991). Thus, based on TOT, a positive relationship between firm age and leverage would be expected. Nevertheless, younger firms may generate insufficient profits (i.e., retained earnings) to finance operational growth (Esperança et al. 2003; Cole 2008; Lopez-Gracia and Sogorb-Mira 2008). If the personal resources of the firm owner(s) are limited, younger firms are forced to take on external debt. In line with this view, most empirical studies (see e.g., Michaelas et al. 1999; Cole 2008) observe a negative relationship between firm age and leverage. This leads to the following hypothesis:

H4: Firm age is negatively related to leverage.

A number of studies demonstrate that the majority of loans to SMEs are collateralized (see e.g., Berger and Udell 1990; Harris and Raviv 1991; Kon and Storey 2003). The use of collateral is aimed at reducing agency problems (related to adverse selection and moral hazard) between the shareholder and the lender (Stiglitz and Weiss 1981). As argued in the literature, tangible assets will be easier to collateralize (as compared to intangibles) given that they usually have reasonably active secondary markets and less uncertain values in distress situations (Hutchinson

1993). Debt covenants are therefore typically written in terms of tangible assets and often explicitly exclude intangibles (Long and Malitz 1992). Based on these arguments, firms with more tangible assets will have easier access to external debt. Moreover, a firm will try to maximize the issuance of secured debt vis-à-vis unsecured debt because the agency costs (and hence cost of capital) of the former are lower. In sum, firms with more tangible assets are expected to have a higher debt ratio. In spite of conflicting evidence (see e.g., Esperança et al. 2003), most empirical findings are consistent with the aforementioned expectation (see e.g., Michaelas et al. 1999; Sogorb-Mira 2005; Heyman et al. 2008). We therefore hypothesize:

H5: Asset tangibility is positively related to leverage.

It is also common to control for profitability when modelling SME financial structure. Based on TOT, a positive relationship between leverage and profitability is expected because (i) high(er) profits tend to be associated with low(er) default risk; and (ii) the higher the profitability of the firm, the more taxes that can be avoided by using debt (Cole 2008; Heyman et al. 2008; Psillaki and Daskalakis 2008). In contrast, a negative relationship is expected based on POT because profitable firms have more internally generated funds, which are preferred over debt and equity financing (Cole 2008; Heyman et al. 2008; Psillaki and Daskalakis 2008).² In support of POT, most empirical studies observe a negative relationship between leverage and firm profitability (see e.g., Van der Wijst and Thurik 1993; Pindado et al. 2006; Heyman et al. 2008). Based on these findings, we hypothesize:

H6: Profitability is negatively related to leverage.

Firms with high growth opportunities are assumed to have higher expected costs of financial distress because the value of these growth opportunities, which can be considered an intangible, is likely to be lost in case of financial distress (Cole 2008). Thus, consistent with TOT, one would predict a negative relationship between leverage and growth. Agency theory would also predict that high growth firms have a lower debt ratio because information asymmetries are more severe for high growth

² Note that a negative relationship is also consistent with firms signalling future results by using more or less debt (Ross 1977).

firms than for low growth firms. Nevertheless, growth also creates a need for resources, which is likely to exhaust internal funds (Michaelas et al. 1999; Psillaki and Daskalakis 2008). Based on this line of thought, high growth firms (or firms with better growth prospects) are more likely to turn to external funds. Whereas this implies a loss of control on behalf of the owner, it is conceivable that the owner will be more assenting to curtail its control aversion if growth is perceived to be essential to the firm's survival (Berggren et al. 2000). A positive relationship between leverage and growth (prospects), which is consistent with the latter argument, is observed in many prior studies (see e.g., Michaelas et al. 1999; Esperança et al. 2003; Sogorb-Mira 2008). This leads to the following hypothesis:

H7: Growth (prospects) is (are) positively related to leverage.

Several studies report important differences in financing patterns across industries (see e.g., Harris and Raviv 1991; Michaelas et al. 1999; Romano et al. 2001). One possible explanation is that firms target an 'optimal' leverage ratio (as suggested by TOT) and that the 'industry practice' serves as a target (see e.g., Frank and Goyal 2004). In other words, firms aim for a financing structure that represents a consensus on what is appropriate given prevailing circumstances in the industry (Holmes et al. 2003). An alternative explanation is that industry proxies for unobservable factors (e.g., asset risk, asset type, and/or need for external funds) that are correlated with industry (Cole 2008). In this vein, Frank and Goyal (2004), for example, show that omitting industry variables from their leverage regression turns many other firm characteristics significant. Based on the aforementioned considerations, we predict a positive relationship between leverage and median industry leverage:

H8: Median industry leverage is positively related to firm leverage.

3. DATA COLLECTION AND VARIABLES

3.1. Data collection

All data were collected from Bureau Van Dijk's BELFIRST database, which contains financial statement data for Belgian and Luxemburg firms. Although the SME definition is subject to considerable differences in prior studies (see, Psillaki and Daskalakis (2008) for a discussion), there is an increasing tendency to rely on the European Commission SME definition. In line with this definition, we selected firms that meet the following criteria: (i) less than 250 employees; (ii) sales below 40 million EUR; and (iii) total assets below 27 million EUR. Based on these criteria, we obtain an initial sample of 100939 SMEs. Because the BELFIRST database only provides information regarding the auditor for the most recent financial statements, our sample is restricted to 2007. Analogous to Heyman et al. (2008), we exclude firms that belong to the financial or governmental sector because the additional requirements that apply to these sectors (e.g., capital requirements in the financial sector) are likely to impact on their financial structure. In addition, we discard observations with missing values. Doing so, we end up with our final sample of 79097 SMEs.

To mitigate the impact of outliers, reported results are based on winsorized data. Winsorization restates outlying values to the largest non-outlying value. Continuous variables are winsorized at 1% and 99%.

3.2. Variables

In this section, we provide an overview of the definitions of our dependent and independent variables that are used in our SME financial structure model. We measure financial structure (i.e., the dependent variable) based on a broad and narrow definition of leverage. The former is defined as the ratio of total *liabilities* over total assets, while the latter is measured as the ratio of total *debt* (excluding trade credit and other short-term non-debt liabilities) over total assets. Because both measures yield similar results (with an exception for firm size, cf. Section 4), results are only reported based on the broad definition of leverage.

The explanatory variables related to quantity and quality of information are defined as follows:

- Quantity of information (INFO) is measured by means of a dummy variable that takes a value of 1 if the firm filed its 2007 FS using the complete format; and 0 if the abbreviated format of the FS was filed.

- Quality of information (QUALITY) is measured by means of a dummy variable that takes a value of 1 if the firm's 2007 FS are audited; and 0 if the FS are not audited.

For the other explanatory variables, we use proxies that have been frequently employed in the literature:³

- Firm size (SIZE) is measured as the natural logarithm of total assets (see e.g., Sogorb-Mira 2005; Heyman et al. 2008).
- Firm age (AGE) is defined as the natural logarithm of the number of years since the incorporation of the firm (see e.g., Cole 2008).
- Asset structure (AS) is measured as the ratio of tangible assets (net fixed assets and inventories) over total assets (see e.g., Sogorb-Mira 2005).
- Profitability (PROF) is defined as return on total assets, being the ratio of earnings before interest and taxes (EBIT) over total assets (see e.g., Michaelas et al. 1999; Sogorb-Mira 2005).
- Growth is defined in two ways. PGROWTH is measured as the geometric average of the yearly growth in total assets over the last 3 years (see e.g., Michaelas et al. 1999; Scherr and Hulburt 2001; Esperança et al. 2003). FGROWTH is defined as the ratio of intangible assets over total assets (see e.g., Michaelas et al. 1999; Esperança et al. 2003; Sogorb-Mira 2005). Whereas the former variable captures past growth, the latter variable proxies for growth prospects.
- Industry (IND) is defined as median industry leverage. Following the Campbell (1996) industry classification, we consider 12 industry groups.

Table I presents the descriptive statistics. The high mean 'broad' leverage of 71.39% can be explained by the creditor-oriented environment in Belgium. Heyman et al. (2008) reported a comparable figure of 68.7% based on a more restricted sample. The maximum leverage of 318.26% indicates that some SMEs in our sample have large retained losses on their balance sheet (i.e., negative equity). About 10% of the SMEs filed their FS according to the full format, while about 11% of the SMEs have their FS externally audited. With respect to asset structure, we find that, on average,

³ As a robustness check, we considered alternative proxies for firm size, asset structure and industry. Firstly, we also considered the natural logarithm of the number of employees as a measure of firm size. Secondly, asset structure was also measured as the ratio of net fixed assets over total assets (inspired by the belief that fixed assets are more secure than current assets (see e.g., Van der Wijst and Thurik 1993)). Finally, we also employed industry dummies to capture the industry effect. Results are robust to these alternative specifications.

intangibles account for about 1.5% of total assets, whereas tangible assets represent about 47% of total assets. These values come close to those reported in prior studies (see e.g., Sogorb-Mira 2005; Heyman et al. 2008). While average profitability is moderate (i.e., 2.75%), our sample firms show a strong average growth of total assets (i.e., 14.13%).

(INSERT TABLE I ABOUT HERE)

Table II presents the correlation matrix. Quite surprisingly, both quantity and quality of information are negatively related to leverage (at the 1% significance level), which is inconsistent with H1 and H2. This negative relationship might (partially) reflect the impact of firm size, given that the legal criteria related to the FS format and the external FS audit are defined in terms of firm size. The strong positive relationship of the information variables with firm size, and the negative relationship of firm size with leverage (all statistically significant at the 1% level) are consistent with this explanation. Our multivariate analyses will provide a more definite answer as we will test the impact of both quantity and quality of information on leverage while controlling for firm size. As the correlation between firm size and the aforementioned variables is well below 0.60, a multivariate model that includes all of these variables should not give rise to multicollinearity problems. However, we should be cautious to include the two information variables together in our model given their high correlation (i.e., 81%), which might give rise to multicollinearity problems (i.e., inflated standard errors of estimated variables). We will therefore explicitly test for multicollinearity and conduct sensitivity tests. The very strong relationship between the information variables arises because the legal criteria that prescribe whether a firm has to disclose FS according to the full format and whether a firm's FS have to be externally audited are identical. Nevertheless, because certain SMEs that disclose the abbreviated format voluntarily opt for an external FS audit, the correlation is not perfect. With a view to being complete, we add that the correlations between leverage and the other independent variables all have the predicted sign and that they all attain statistical significance at the 1% level.

(INSERT TABLE II ABOUT HERE)

4. METHOD OF ANALYSIS AND EMPIRICAL RESULTS

The hypotheses developed in Section 2 are empirically tested based on the following OLS regression model:

$$LEVERAGE = \beta_0 + \beta_1 INFO + \beta_2 QUALITY + \sum_{i=3}^9 \beta_i CONTROL_i + \varepsilon$$

with $CONTROL = \{SIZE; AGE; AS; PROF; PGROWTH; FGROWTH; IND\}$.

Results for our OLS regression model are reported in Table III (cf. Model I). A quick look at Table III indicates that coefficients for all independent variables attain statistical significance at the 1% level. This observation is supported by the joint F-test, which indicates (i.e., based on its statistical significance) that from a statistical point of view all variables need to be considered in our model.

Unlike results based on bivariate correlations (cf. supra), coefficients for the variables related to both information quantity and quality have the predicted signs. This change in signs for both variables provides support for our earlier argument that both variables also (partially) capture a size effect. The observed positive coefficients are consistent with H1 and H2 and support the view that lack of (quality) information inhibits firms from using external funds because it increases the cost of external funding. Despite the high correlation between both aforementioned variables (cf. supra), variance inflation factors (VIFs) do not suggest multicollinearity problems (i.e., the VIFs are 3.274 and 3.259, respectively). Nevertheless, as a robustness check, we estimated two alternative models (i.e., Model II and Model III in Table III) based on two sub-samples. In Model II, we drop the information quality variable and re-estimate our model for a sub-sample that includes all SMEs with externally audited FS. Estimating this model, we test the impact of quantity of information on leverage while controlling for information quality (i.e., in this sub-sample the quality of information is held constant). In Model III, we drop the information quantity variable from our basic model, and re-estimate the model for a sub-sample composed of all SMEs with abbreviated FS. Doing so, we are able to test the impact of information quality on leverage while controlling for the quantity of information

(i.e., in this sub-sample information quantity is held constant). As can be seen from Table III, all coefficients are stable across the three models and our results are therefore robust.

(INSERT TABLE III ABOUT HERE)

In accordance with the results on the financial structure of Belgian SMEs reported in Heyman et al. (2008), we obtain a significantly negative coefficient for firm size in all three regressions (which is consistent with H3). Whereas both TOT and POT predict a positive relationship, firm size is a difficult variable to interpret, as it may capture different effects (Heyman et al. 2008). For example, in our sample (see Table II), firm size is significantly positively related to firm age and profitability. Thus, one potential explanation for the observed negative relationship is that large firms have more internally generated funds (i.e., retained profits) that are subsequently used to finance the firm. However, if we measure leverage based on the narrow definition, we obtain a significantly positive coefficient for firm size. In sum, these findings suggest that large firms use fewer liabilities, but rely more heavily on (financial) debt. The latter is consistent with large firms having easier access to financial debt thanks to lower probabilities of default and less severe information asymmetry problems. Small firms have more difficulties obtaining debt and will therefore be more dependent upon other types of liabilities (e.g., trade credit, advance payments from clients, etc.).

In line with the argument that more mature firms will rely more on internal financing, we observe a significantly negative coefficient for firm age (which is consistent with H4). Whereas TOT, predicts a positive relationship because older firms are more reputed, our results support the view that younger firms rely more heavily on liabilities because profits are insufficient to finance the firm's operational growth. In a similar vein, and consistent with H6, we observe a significantly negative relationship between leverage and profitability.

The significantly positive coefficient on the asset structure variable is consistent with H5 (and TOT) and supports the view that firms with more tangible assets will have easier access to external debt.

Consistent with POT, the two growth variables are significantly positively related to leverage. As discussed earlier (cf. Section 2), whereas it is argued that the expected costs of financial distress are higher for growth firms, growth creates a need for resources, which is likely to exhaust internal funds and thus force growth firms to turn to external funds.

Finally, we confirm the industry effect documented in prior studies. The significantly positive coefficient on median industry leverage is both consistent with firms targeting an optimal leverage ratio (where the 'industry practice' serves as a target) and/or industry being a proxy for unobservable factors that are correlated with industry. While both explanations are plausible, they are based on markedly different grounds. Nevertheless, based on our analyses, we are not able to determine which explanation actually applies.

5. CONCLUSIONS

Based on a broad sample of Belgian SMEs, we have formally tested the impact of differences in quantity and quality of information on SME financial structure. In line with traditional asymmetric information arguments, our results show that both information quantity and quality are positively related to SME leverage. Our results therefore support the view that lack of information and low information quality inhibits firms from using external funds. SMEs with more extensive information and/or higher information quality rely more heavily on liabilities, which is consistent with these firms having a lower cost of external capital. These findings have practical relevance, as they indicate that Belgian SMEs are able to reduce the cost of external financing by providing more information and/or information of a higher quality. Firms that are not subject to a mandatory external FS audit, for example, could opt for a voluntary external FS audit in order to reduce the cost of external capital.

Secondly, because the results for our control variables are consistent with prior studies, we conclude that the financial behaviour of Belgian SMEs is comparable to that of SMEs in other developed countries. Specifically, we find that leverage is positively related to asset structure, growth (prospects) and median industry leverage; and negatively related to firm age and profitability. Results for firm size are ambiguous and depend on whether a broad or narrow leverage definition is used. Last but not least, our findings indicate that the traditional capital structure theories (i.e., POT, TOT and agency theory) are all relevant in explaining Belgian SME capital

structures. For example, whereas the observed negative relationship between profitability and leverage is consistent with POT, the significantly positive coefficient for median industry leverage provides support for TOT. Our results are also consistent with agency theory, as we observe a positive relationship between asset tangibility and leverage. Therefore, as argued by Myers (2001), we confirm that no single theory gives a general explanation of firms' financing strategies.

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TABLE I: Descriptive statistics

Variable	Mean	Std. Dev.	Minimum	Maximum
LEVERAGE	0.7139	0.4432	0.0515	3.1826
INFO	0.1017	0.3022	0	1
QUALITY	0.1133	0.3171	0	1
SIZE	6.7978	1.3893	2.9444	9.7188
AGE	2.6495	0.6646	0.6931	4.0943
AS	0.4671	0.2674	0	0.9740
PROF	0.0275	0.1551	-0.9375	0.4717
PGROWTH	0.1413	0.3301	-0.2557	2.1492
FGROWTH	0.0149	0.0620	0	0.5351
IND	0.7241	0.0454	0.6724	0.8293

LEVERAGE = total liabilities/total assets; INFO = dummy variable that takes a value of 1 if the firm filed its FS using the complete format, and 0 otherwise; QUALITY = dummy variable that takes a value of 1 if the firm's FS are audited, and 0 otherwise; SIZE = $\ln(\text{total assets})$; AGE = $\ln(\text{number of years since the incorporation of the firm})$; AS = tangible assets/total assets; PROF = earnings before interest and taxes/total assets; PGROWTH = geometric average of the yearly growth in total assets over the last 3 years; FGROWTH = intangible assets/total assets; IND = median industry leverage.

TABLE II: Correlation coefficients

	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)	(10)
LEVERAGE (1)	1.00									
INFO (2)	-0.03 ***	1.00								
QUALITY (3)	-0.04 ***	0.81 ***	1.00							
SIZE (4)	-0.23 ***	0.49 ***	0.48 ***	1.00						
AGE (5)	-0.21 ***	0.15 ***	0.18 ***	0.31 ***	1.00					
AS (6)	0.17 ***	-0.15 ***	-0.14 ***	0.00	-0.01	1.00				
PROF (7)	-0.50 ***	0.03 ***	0.03 ***	0.19 ***	0.07 ***	-0.16 ***	1.00			
PGROWTH (8)	0.06 ***	-0.01 **	-0.01 ***	0.08 ***	-0.17 ***	-0.02 ***	0.06 ***	1.00		
FGROWTH (9)	0.09 ***	-0.04 ***	-0.04 ***	-0.08 ***	-0.25 ***	-0.16 ***	-0.05 ***	0.02 ***	1.00	
IND (10)	0.17 ***	-0.05 ***	-0.05 ***	-0.18 ***	-0.08 ***	0.15 ***	-0.13 ***	-0.03 ***	0.05 ***	1.00

LEVERAGE = total liabilities/total assets; INFO = dummy variable that takes a value of 1 if the firm filed its FS using the complete format, and 0 otherwise; QUALITY = dummy variable that takes a value of 1 if the firm's FS are audited, and 0 otherwise; SIZE = $\ln(\text{total assets})$; AGE = $\ln(\text{number of years since the incorporation of the firm})$; AS = tangible assets/total assets; PROF = earnings before interest and taxes/total assets; PGROWTH = geometric average of the yearly growth in total assets over the last 3 years; FGROWTH = intangible assets/total assets; IND = median industry leverage.

* denotes statistical significance at the 10% level

** denotes statistical significance at the 5% level

*** denotes statistical significance at the 1% level

TABLE III: Regression results

	Model I	Model II	Model III
Intercept	0.5805 (24.13)***	0.8875 (13.90)***	0.6130 (27.19)***
INFO	0.1133 (14.55)***	0.0732 (7.68)***	
QUALITY	0.0512 (6.93)***		0.0725 (8.53)***
SIZE	-0.0470 (39.50)***	-0.0366 (10.41)***	-0.0487 (40.47)***
AGE	-0.0780 (36.63)***	-0.0532 (9.57)***	-0.0791 (36.23)***
AS	0.2030 (39.79)***	0.0463 (3.20)***	0.2143 (41.75)***
PROF	-1.1513 (132.06)***	-1.0834 (45.39)***	-1.1364 (127.69)***
PGROWTH	0.3062 (14.05)***	0.1522 (2.15) **	0.3291 (16.76)***
FGROWTH	0.1028 (25.37)***	0.0830 (6.70)***	0.1069 (26.18)***
IND	0.7407 (24.92)***	0.2817 (3.60)***	0.7051 (25.49)***
<i>Adjusted R²</i>	<i>28.70%</i>	<i>21.89%</i>	<i>28.97%</i>
<i>F (p-value)</i>	<i>3542.12 (0.000)</i>	<i>334.35 (0.000)</i>	<i>3902.53 (0.000)</i>
<i>Number of obs.</i>	<i>79079</i>	<i>8965</i>	<i>71052</i>

LEVERAGE = total liabilities/total assets; INFO = dummy variable that takes a value of 1 if the firm filed its FS using the complete format, and 0 otherwise; QUALITY = dummy variable that takes a value of 1 if the firm's FS are audited, and 0 otherwise; SIZE = ln(total assets); AGE = ln(number of years since the incorporation of the firm); AS = tangible assets/total assets; PROF = earnings before interest and taxes/total assets; PGROWTH = geometric average of the yearly growth in total assets over the last 3 years; FGROWTH = intangible assets/total assets; IND = median industry leverage.

Absolute values of t-statistics are reported in parentheses.

* denotes statistical significance at the 10% level

** denotes statistical significance at the 5% level

*** denotes statistical significance at the 1% level