The Influence of Debt Financing Structure on Corporate Financial Risk

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Abstract. The consistent increase in corporate leverage ratios in China has raised concerns about systemic risks. Using A-share non-financial listed companies from 2015 to 2024 as a sample, this paper empirically examines the impact of debt financing structure on corporate financial risk and its variation across industries. The study finds that: First, debt financing structure is positively correlated with corporate financial risk, meaning an increase in the debt financing ratio significantly exacerbates corporate financial risk; Second, compared to asset-heavy industries, the positive impact of the debt financing structure on corporate financial risk is more pronounced in asset-light industries. This research provides a theoretical basis for differentiated corporate leverage control policies.

Keywords: Debt Financing Structure, Corporate Financial Risk, Industry Characteristics, Fixed Effects Model.

1. Introduction

In recent years, the debt issues of Chinese firms have continued to attract significant attention from regulators. The People's Bank of China has repeatedly warned that the leverage ratios in certain industries have "exceeded warning levels," indicating accumulating potential financial risks. Macroeconomics data shows that the leverage ratio of China's non-financial corporate sector remained at a relatively high level in 2024, while significant variation exists among firms at the micro level. Excessive debt levels have created a series of operational challenges for firms. For instance, asset-light firms heavily reliant on short-term debt financing have experienced financial distress due to cash flow disruptions, highlighting the severe impact of imbalanced debt structures on financial stability. Against this backdrop, an in-depth exploration of how corporate debt financing structures influence their financial risks has practical implications for optimizing corporate financing decisions, avoiding bankruptcy crises, and enabling regulators to accurately identify and prevent systemic financial risks.

Scholars have long examined the relationship between debt financing structure and corporate financial risk. Numerous studies have explored how debt maturity structures and types influence corporate value and risk-taking behaviors, with theoretical frameworks such as the tax shield effect and agency costs explaining the underlying mechanisms. However, existing literature predominantly focuses on dimensions such as debt maturity and type, while systematic research on the debt financing ratio remains relatively limited. Whether and how the debt financing ratio can comprehensively reflect a firm's debt burden and repayment capacity still requires further investigation.

Building on this foundation, this study systematically examines the impact of the debt financing structure on corporate financial risk. The core research questions are: (1) Does debt financing structure affect corporate financial risk? (2) Are there differences in this impact between asset-light and asset-heavy industries? Using data from non-financial A-share listed companies from 2015 to 2024, the empirical analysis yields two key findings: First, an increased debt financing ratio significantly amplified financial risks; Second, this risk-amplifying effect is notably stronger in asset-light industries than in asset-heavy sectors. These conclusions provide a crucial theoretical and empirical foundation for developing differentiated risk prevention strategies.

2. Literature review

2.1. Economic consequences of debt financing structure

The debt financing structure refers to a firm's method of raising funds through various debt instruments. Its core dimensions include the debt maturity structure (the balancing short-term and long-term liabilities), the debt type structure (bank loans, bonds, commercial credit), and the leverage ratio (asset-liability ratio) [1]. The economic consequences of debt financing structures encompass multiple aspects, including impacts on the firm itself, financial markets, and the broader macroeconomy.

The impact of the debt financing structure on corporate performance and risk has both positive and negative dimensions. On the positive side, debt financing can enhance firm value through the tax shield effect [2], where pre-tax interest payments reduce taxable income, and the scale of debt is directly proportional to the tax-deductible benefits. Simultaneously, it generates financial leverage advantages: a well-structured debt financing framework during profitable periods can amplify shareholder returns while lowering the overall capital costs, thereby boosting corporate value [3]. Moreover, debt financing helps mitigate equity agency conflicts and reduce agency costs [4], as firms may incentivize managers to align with shareholder interests through mechanisms such as stock buybacks. On the negative side, an imbalanced debt financing structure may trigger financial distress costs, increasing corporate financial pressure that could lead to crises or bankruptcy [5]. Additionally, such structural imbalances exacerbate debt agency conflicts between shareholders and creditors. Shareholders pursuing high-risk returns might engage in asset substitution [4] or underinvestment [6], resulting in heightened agency costs and tighter financing constraints.

At the financial market level, debt financing structures can influence market stability through signaling mechanisms. For instance, an excessively high debt-to-asset ratio may signal financial vulnerabilities to the market [7], triggering a decline in investor confidence, increased financing costs,and heightened market uncertainty. Simultaneously, multiple corporate defaults could spark credit crises that disrupt normal financial operations. From a macroeconomic perspective, debt financing impacts fiscal sustainability and resource allocation efficiency – for example, excessive government debt accumulation intensifies repayment pressures and increases long-term fiscal crisis risks [8]. Moreover, debt cycles are correlated with economic cycles, with distinct debt financing patterns corresponding to different phases of economic development. When speculative or Ponzi-style debt financing [9] accounts for an excessive proportion at the national or sectoral level, it may escalate financial risks and potentially trigger systemic financial instability.

2.2. Factors influencing corporate financial risk

Corporate financial risk manifests as declining profitability or bankruptcy risk stemming from debt pressure, cash flow fluctuations, or insufficient debt repayment capacity [10]. Existing research categorizes factors influencing financial risk into two types: internal governance and the external environment. Internal factors primarily include an imbalanced debt financing structures [11][12], corporate governance mechanisms [13], and internal control quality [14]. Among these, an imbalanced debt financing structure serves as a core internal risk source. Excessive reliance on short-term debt directly escalates liquidity risk [15], particularly for asset-light industries [16] like media firms [17], where high-cost short-term liabilities can easily trigger liquidity crises. An excessively high debt-to-asset ratio reduces corporate investment and borrowing capacity through the debt overhang effect, potentially leading to bankruptcy risk [18]. Corporate governance also moderates risk transmission. Sound governance mechanisms can partially mitigate risks—firms with higher proportions of independent directors and reasonable ownership concentration effectively curb controlling shareholders' tunneling [19], thereby reducing financial risk. Firms where executives hold significant shares show a negative correlation with financial risk, meaning greater executive ownership is associated with lower financial exposure [20]. Conversely, firms with high equity pledge ratios face intensified risks due to agency problems [19].

External factors encompass both the policy environment and industry-specific characteristics. The policy environment influences risk levels through restrictions or incentives on financing channels [21]. When environmental policy uncertainty is high, companies tend to increase short-term financial asset holdings while reducing long-term debt ratios to mitigate financial risks. However, high-leverage firms have a limited capacity for such risk mitigation [22]. For instance, under joint disciplinary systems for credit violations, firms may turn to informal financing. While this provides temporary relief from constraints, it carries higher default risks in the long run [23]. Industry-specific differences also play a significant role. In asset-light sectors like the media industry, where fixed assets available for collateral are scarce, creditors impose higher risk premiums. Consequently, increased debt financing ratios may suppress corporate performance [17][24].

2.3. Literature review and commentary

Existing research has conducted in-depth explorations into the economic consequences of debt financing structures and the internal and external factors influencing corporate financial risk, establishing a solid foundation for this study. However, while a systematic analysis of how the debt financing structure affects corporate financial risk remains insufficient. Therefore, this paper focuses on the debt-to-asset ratio—a core indicator of the debt financing structure—to thoroughly analyze its influence on corporate financial risk, aiming to shed light on the overall impact of the debt financing structure on corporate financial stability.

3. Theoretical analysis and research hypothesis

In general, a firm's debt financing structure affects its financial risk through mechanisms such as the tax shield effect [25], agency costs [26], signaling [27], and the debt overhang effect [28].

As the proportion of debt financing rises, the asset-liability ratio increases, and the benefits from the tax shield effect gradually diminish. Meanwhile, excessive debt levels may lead to a decline in corporate credit ratings and higher financing costs, offsetting some of the gains from the tax shield [29]. Additionally, high debt levels can trigger market concerns, eroding investor confidence and further impairing corporate financing capabilities. From the perspective of agency costs, conflicts of interest between shareholders and creditors exist regardless of the level of debt. When corporate debt becomes excessive, management may face greater pressure to take risks to address debt burdens and pursue higher returns. This increases exposure to risks – if high-risk projects fail, cash flow deteriorates and financial risk escalates. Simultaneously, high debt ratios may cause management to abandon investment projects with a positive net present value (NPV) to avoid default risk, leading to underinvestment, missed opportunities, declining long-term profitability, weakened debt repayment capacity, and increased financial risk. Moreover, excessive debt financing elevates the asset-liability ratio, signaling poor financial health to investors and creditors. These negative signals increase financing costs, damage corporate reputation, and worsen financial conditions. As corporate debt levels rise, the debt overhang effect emerges as a key risk mechanism [28]. High interest expenses crowd out operating cash flows, potentially trapping firms in a vicious cycle. Firms may be forced to rely on short-term debt rollovers to maintain operations, and their financial situation can gradually deteriorate in the long run. Debt overhang can also inhibit firms' willingness to undertake long-term investment, weaken their core competitiveness, and thus increase their financial risk.

Based on the above theoretical analysis, this paper proposes Hypothesis 1:

H1: The debt financing structure is positively correlated with corporate financial risk; that is, a higher proportion of debt financing corresponds to greater financial risk.

Notably, the impact of the debt financing structure on corporate financial risk is moderated by both the internal and external business environment. Well-managed firms can more effectively curb short-sighted and risky behaviors by management, ensure transparent and high-quality information disclosure, and strengthen investor and creditor confidence, thereby cushioning the impact of high leverage to some extent. Externally, industry heterogeneity also plays a crucial role. Sectors with

strong asset liquidity and stable profitability demonstrate greater resilience to high debt burdens [30]. In asset-heavy industries where fixed assets constitute a large proportion of the balance sheet, sufficient collateral can reduce creditors' risk premiums and enable refinancing through asset pledges during cash flow shortages, creating a buffer against risk. Conversely, asset-light industries face challenges in reducing financing costs through collateral due to their lower fixed asset ratios. Moreover, their cash flows are more susceptible to market fluctuations, making them more vulnerable to the impacts of high leverage.

Based on the above theoretical analysis, this paper proposes Hypothesis 2:

H2: Compared with asset-heavy industries, the debt financing structure in asset-light industries has a more significant positive impact on corporate financial risk.

4. Research design

4.1. Sample selection and data sources

This study examines A-share listed companies from 2015 to 2024. The sample selection follows these criteria: (1) Excluding financial firms; (2) Removing ST and *ST companies; (3) Excluding observations with missing key variables or discontinuous annual data. The final dataset comprises 21,340 unbalanced panel observations. To ensure robustness and mitigate the impact of outliers, we winsorized all continuous variables at the 1st and 99th percentiles. All data were sourced from the CSMAR (China Stock Market & Accounting Research) database or calculated based on data therefrom.

4.2. Model construction and variable definition

To examine the impact of the debt financing structure on corporate financial risk, we establish the following empirical model:

$$DZ_{i,t} = \alpha_0 + \alpha_1 Lev_{i,t} + \alpha_i Controls_{i,t} + \sum Year + \sum Industry + \varepsilon_{i,t} \quad (1)$$

In this model, the subscripts i and t represent the firm and year, respectively. The variables are defined as follows.

(1) Dependent Variable: Corporate financial risk. This study employs the Z-score, following the research of Chen et al. (2021), to measure corporate financial risk. The calculated Z-score inversely indicates the severity of financial risk – a higher Z-score signifies lower financial risk. The Z-score is calculated as follows:

$$Z = 1.2X_1 + 1.4X_2 + 3.3X_3 + 0.6X_4 + 0.999X_5 \quad (2)$$

The components are: X1= Working capital/Total assets; X2= Retained earnings/Total assets; X3= Earnings before interest and taxes/Total assets; X4= Market value of equity/Total book liabilities; X5= Sales revenue/Total assets.

Explanatory Variable: Debt financing structure. Among the multiple dimensions of debt financing structure, this study selects the asset-liability ratio (total liabilities divided by total assets) as the core proxy. A higher asset-liability ratio indicates a greater reliance on debt financing.

(3) Control Variables: Following the research by Kang et al. (2025) and He (2023), this study further controls for other factors that may influence corporate financial risk, including firm size (Size), development capability (Growth), return on total assets (ROA), board size (Bsize), the proportion of independent directors (Indep), and the shareholding ratio of the top ten shareholders (Top10). Additionally, year and industry fixed effects are controlled. Detailed definitions are presented in Table.1.

Table.1. Variable Definitions

Type of variable	Variable name	Variable symbol	Variable definition
Dependent variable	Corporate financial risk	DZ	The larger the Z value, the smaller the financial risk of the firm
Independent variable	Debt financing structure	Lev	Debt-to-asset ratio = total liabilities/total assets
Control variable	Firm size	Size	Natural logarithm of total assets at the end of the period
	Capacity for development	Growth	Annual growth rate of operating income
	Return on assets	ROA	Net profit/total assets
	Board size	Bsize	Total number of directors
	Independent director ratio	Indep	Number of independent directors/Total number of directors
	Shareholding ratio of the top ten shareholders	Top10	The shareholding ratio of the firm's top ten shareholders

5. Empirical analysis

5.1. Descriptive statistics

Table.2. presents the descriptive statistics for all variables in Model (1). The mean value of financial risk (DZ) is 5.719 with a standard deviation of 8.798, ranging from -77.514 to 420.399, indicating substantial variation in financial risk levels across the sample firms. The debt financing structure (Lev) has a mean of 43.3% and a standard deviation of 19.4%, while extreme values reaching 99%, which corroborates regulatory warnings about corporate leverage exceeding safety thresholds. The natural logarithm of firm size (Size) has a mean of 13.455 and a standard deviation of 1.377, reflecting the sample's inclusion of large, medium, and small-sized listed companies. The return on assets (ROA) averages 3.2%, and the proportion of independent directors (Indep) stands at 37.7%, consistent with the governance structure characteristics of Chinese listed companies. Notably, the average shareholding ratio of the top ten shareholders (Top10) reaches 55.4%, indicating a high degree of ownership concentration.

Table.2. Descriptive statistics

Variable	N	Average Value	Standard Error	Least Value	Crest Value
DZ	21340	5.719	8.798	-77.514	420.399
Lev	21340	0.433	0.194	0.013	0.990
Size	21340	13.455	1.377	8.088	19.580
Growth	21340	0.280	12.996	-1.309	1880.750
ROA	21340	0.032	0.072	-1.648	0.786
Bsize	21340	8.519	1.667	0.000	18.000
Indep	21340	0.377	0.060	-0.444	1.095
Top10	21340	55.397	16.068	1.320	319.530

5.2. Correlation analysis

Table.3. presents the correlation matrix. The debt financing structure (Lev) is significantly negatively correlated with corporate financial risk (DZ) at the 1% level. However, because a higher Z-score indicates lower risk, this negative correlation demonstrates a significant positive relationship between the debt financing structure (Lev) and corporate financial risk (DZ). These preliminary findings support Hypothesis 1.

Table.3. Correlation analysis results

Variable	DZ	Lev	Size	Growth	ROA	Bsize	Indep	Top10
DZ	1.000							
Lev	-0.459* (0.000)	1.000						
Size	-0.270* (0.000)	0.490* (0.000)	1.000					
Growth	-0.004 (0.580)	0.020* (0.004)	0.026* (0.000)	1.000				
ROA	0.195* (0.000)	-0.281* (0.000)	0.062* (0.000)	0.006 (0.348)	1.000			
Bsize	-0.093* (0.000)	0.117* (0.000)	0.246* (0.000)	0.025* (0.000)	0.041* (0.000)	1.000		
Indep	0.022* (0.001)	0.012 (0.074)	0.052* (0.000)	-0.004 (0.512)	-0.011 (0.112)	-0.480* (0.000)	1.000	
Top10	-0.013* (0.050)	0.015* (0.029)	0.216* (0.000)	0.025* (0.000)	0.197* (0.000)	0.104* (0.000)	0.007 (0.330)	1.000

Note: ***, *, and * indicate significance at the 1%,5%, and 10% levels, respectively; the values in parentheses are robust t-values adjusted for heteroskedasticity, as is the case below.

5.3. Multicollinearity Test

The results of the multicollinearity test are presented in Table.4. According to the results in Table.4, the mean value of VIF is 1.307, and the VIF for each variable is well below the common threshold of 5, suggesting that multicollinearity is not a serious concern.

Table.4. Multicollinearity Test Results

	Variance Expansive Factor (VIF)	1/ variance inflation factor
Lev	1.513	0.661
Size	1.557	0.642
Growth	1.002	0.998
ROA	1.182	0.846
Bsize	1.443	0.693
Indep	1.356	0.738
Top10	1.093	0.915
Mean variance expansion factor	1.307	0.765

5.4. Hausman test

Table.5 reports the results of the Hausman test for model (1). According to the results in Table.5, the p-value of the test is 0.0001, which is statistically significant at the 1% level. Therefore, the fixed-effects model is preferred and used for the benchmark regression.

Table.5. Hausman test results

	Coefficient
Chi-square test value	106.81
P price	0.0001

5.5. Regression analysis

Table.6 presents the results of the fixed-effects regression based on Model (1). The coefficient on the debt financing structure (Lev) is -15.777 and is statistically significant at the 1% level (t= -30.43). This implies that a one-unit increase in the debt-to-asset ratio decreases the Z-score by 15.777 units. Given that a lower Z-score signifies higher risk, this result indicates a significant increase in financial risk. These findings support Hypothesis H1, confirming that a higher debt financing ratio is associated with greater corporate financial risk.

Table.6. Regression analysis results

	DZ
Lev	-15.777***
	(-30.430)
Size	-1.750***
	(-16.568)
Growth	-0.000
	(-0.050)
ROA	8.901***
	(12.187)
Bsize	-0.070
	(-1.199)
Indep	2.085
	(1.572)
Top10	-0.009*
	(-1.704)
Constant	36.150***
	(22.024)
Year&Ind	control
N	21340
R2	0.104
F	319.266

5.6. Robustness test

(1) Sub-sample analysis

To account for potential variations across different macroeconomic cycles, we conduct a robustness check using a subsample from a more recent period. Specifically, we re-run the regression using data from 2020 to 2024. As shown in Table.7(1), the debt financing structure (Lev) shows a statistically significant negative correlation with corporate financial risk (DZ) at the 1% level,

consistent with the main regression results in Table.6. This demonstrates that the research conclusions is robust across different time periods.

(2) Winsorization

To further reduce the potential influence of extreme values in regression results, we applied a more stringent Winsorization technique, truncating continuous variables at the 20th and 80th percentiles. The regression results after this adjustment are presented in column (2) of Table.7. The relationship between the debt financing structure (Lev) and corporate financial risk (DZ) remains highly significant at the 1% level. Although the magnitude of the coefficient estimate changed due to the different treatment of outliers, the strong inverse relationship remains highly consistent with the main regression results. This provides robust evidence that the identified positive impact of the debt financing structure on financial risk is not driven by extreme values, thereby confirming the robustness of our findings.

(3) Lagged explanatory variable

To mitigate potential reverse causality concerns (e.g., the possibility that lower financial risk facilitates easier access to loans), we re-estimate the model using the one-period lagged value of the leverage ratio. As shown in Column (3) of Table.7, the coefficient on the lagged leverage ratio (L. Lev) remains negative and statistically significant at the 1% level, which reinforces the core conclusion of H1 and alleviates endogeneity concerns.

Table.7. Regression analysis results after sample reduction (2020-2024)

	(1) Sample reduction	(2) Tail retraction treatment	(3) Lag phase
	DZ	DZ	DZ
Lev	-12.301***	-7.154***	
	(-17.053)	(-28.479)	
L.Lev			-8.574***
			(-17.520)
Size	-2.610***	-1.247***	-1.756***
	(-12.550)	(-29.188)	(-15.441)
Growth	0.006	0.001	-0.064***
	(0.132)	(0.074)	(-2.741)
ROA	7.081***	8.878***	12.905***
	(8.722)	(29.745)	(19.149)
Bsize	-0.094	0.045**	-0.079
	(-1.214)	(2.034)	(-1.341)
Indep	-1.312	2.815***	1.599
	(-0.797)	(5.805)	(1.192)
Top10	-0.003	0.001	-0.030***
	(-0.306)	(0.638)	(-5.203)
Constant	47.468***	22.233***	34.112***
	(15.661)	(33.870)	(19.401)
Year&Ind	control	control	control
N	10670	12805	19206
R2	0.087	0.261	0.437
F	116.610	552.638	13225.993

5.7. Heterogeneity analysis

To test Hypothesis H2 regarding industry heterogeneity, we follow established practice by classifying industries based on asset intensity. We calculate the median of the average total assets for each industry. Industries with an average asset size above the median are classified as asset-heavy, while those below the median are classified as asset-light. The results from the subgroup regressions

reveal that the coefficient on Lev for the asset-light industry group is -84.864 (t-statistic = -59.27), which is significantly larger in absolute magnitude than the coefficient for the asset-heavy group. The difference between these two coefficients is statistically significant based on a Seemingly Unrelated Regression (SUR) test (χ^2=36.71, $p-value < 0.01$). This finding is consistent with the hypothesis that asset-light firms, due to their lower proportion of fixed assets usable as collateral, face more severe credit constraints and higher cash flow volatility. The regression results indicate that the effect of the debt financing structure on corporate financial risk is more pronounced in asset-light industries, thus confirming Hypothesis H2. This suggests that policymakers and managers in asset-light industries should consider implementing more stringent leverage control measures.

Table.8. Heterogeneity test results based on industry nature

variable	Light Assets Industry	Heavy assets industry
	DZ	DZ
Lev	-84.864***	-63.579***
	(-59.27)	(-29.690)
Size	-0.762***	-0.358***
	(-11.91)	(-4.540)
Growth	-0.008	-0.001
	(-0.24)	(-0.390)
ROA	14.67***	9.178***
	(15.71)	(4.700)
Bsize	-0.132***	0.147**
	(-2.70)	(2.410)
Indep	0.383	2.990
	(0.28)	(1.530)
Top10	0.016***	-0.011
	(3.59)	(-1.600)
Constant	35.375***	24.219***
	(35.68)	(19.560)
Year&Ind	control	control
N	14563	2142
R^2	0.326	0.441
F	879.516	210.360

6. Research conclusions

This study uses the debt-to-asset ratio as a key proxy for the corporate debt financing structure and empirically examines its impact on financial risk. The analysis yields two main conclusions: (1) The

debt financing structure exhibits a significant positive correlation with corporate financial risk; meaning a higher debt ratio is associated with greater financial risk. (2) This relationship exhibits significant industry heterogeneity. The positive correlation is significantly stronger for firms in asset-light industries compared to those in asset-heavy sectors. Asset-light firms, characterized by lower levels of fixed assets, face challenges in reducing financing costs through asset collateralization. Consequently, these firms exhibit higher bankruptcy risks at elevated leverage levels, highlighting structural vulnerabilities in their ability to withstand financial distress.

These findings have several implications. At the corporate level, firms in asset-light industries should establish stricter internal leverage thresholds to avoid over-reliance on short-term debt rollovers. Asset-heavy firms, while generally more resilient, should still dynamically optimize their debt maturity structures to mitigate refinancing risks. For regulators, it is advisable to implement differentiated leverage warning lines across industries and strengthen cash flow monitoring for asset-light firms. Furthermore, providing targeted long-term low-interest loans could support debt restructuring in high-tech and other viable asset-light sectors, avoiding the adverse effects of one-size-fits-all deleveraging policies on healthy firms. This study has certain limitations. It does not fully address the impact of other dimensions of debt structure, such as debt maturity and type. Future research could extend this work by constructing a comprehensive, multi-dimensional index of financing structure and further exploring its relationship with financial risk.

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