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Consequences of Political Exits on Capital Structure: Brexit Case

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The paper addresses the impacts of political exits on capital structure policies, through studying the impact of the Brexit deal on the UK's companies listed at FTSE 100 as a practical case. The study is divided into two periods: the first before the Brexit deal (2010-2015) and the second after the referendum until Brexit (2016-2021). Data were collected from the annual reports of the UK companies and the FTSE 100 database. Moreover, capital structure policies were studied by analyzing the determinants such as long-term debt over total equity, profitability, tangibility, liquidity, propensity to pay dividends, size, and political factor—Brexit. The results show that there is a direct relationship between political exits and capital structure. Also, the results show that the financial ratios are different between the two periods (before and after Brexit), where it seems that the capital structure variables were affected starting from the referendum period, political negotiations between the two parties, and then Brexit (2016-2021). In addition, the correlation matrix shows that long-term debt over total equity has a negative correlation with profitability, liquidity, and political factors, where it seems that long-term debt over total equity has a positive correlation with tangibility, size, and paying dividends. Moreover, the results show that political shocks were affecting the FTSE 100 performance starting from 2016 until 2021. The study could be useful for financial and economic academics. Moreover, the study could be helpful for EU members and the UK government, taking into consideration the interests of the UK and EU where any future policies or laws will affect the financial and economic sectors of the two parties.

Keywords: capital structure, uncertainty, political exits, Brexit, FTSE 100

Introduction

Political practices have always been associated with economic and financial policy. Political decisions such as referendums, and presidential elections have a lot of consequences on corporate financial policies (Robinson, 1981). Historically, many researchers have analyzed the relationship between politics and finance from different aspects. Hadley (1899) mentions that there is a close relationship between politics and economics that has emerged over the years in most regimes. In the last twenty years, political considerations have played an increasing role in financial strategies in addition to the political connections in firms and the effects of political uncertainty on investments (Zingales, 2017).

The political environment has a historical relation with financial policies, where political practices such as government orientation, election systems, regulations, and revolutions appear to be linked to financial sectors

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and directly influence the decision-making of companies and banks. Governments must provide more stable and democratic systems to maintain economic life by offering an encouraging and competitive work environment, protecting financial markets, facilitating the work of banks to increase investments, supporting more stable startups, and better protecting property rights (Capie, 2001).

Political decisions such as joining or exiting political unions have a great influence on the financial level, where these decisions may cause a lot of consequences on the financial policy and the companies' performance. Thissen et al. (2020) mention that political exits such as Brexit, have a lot of implications for the UK and EU economies, especially for UK companies. Usually, exits happen when one of the participating members wants, for various reasons or considerations, to leave the union. In this context, Huysmans and Crombez (2020) address that throughout history, there have been many cases of countries that exit from their political unions or split into two countries.

In addition to the exit of the UK from the EU in 2020, which is known as Brexit, several countries have been separated around the world in recent history. Among them are the split of South Sudan from Sudan in 2011 and the split of Eritrea from Ethiopia in 1993. According to Acemoglu and Robinson (2012) "States don't fail overnight. The seeds of their destruction are sown deep within their political institutions". In most cases, the idea of separation is born due to harsh conditions such as war and conflicts. However, the UK has other reasons for leaving the EU. Mauldin (2016) stated that there were three main reasons for the exit: economics, sovereignty, and political elitism.

The increase of political and economic crises in Europe and the inability of the member states to develop clear strategies and policies to deal with future dangers, prompted the UK to leave the EU. For sure, the Brexit deal will impact the performance of UK companies and their financial policies, but the question remains to what extent? According to Bloom et al. (2019), Brexit created uncertainty in June 2016. This uncertainty persisted for more time without agreement on the terms of the UK's withdrawal, as companies became more skeptical about the fate and terms of the deal. The UK's exit from the EU was a political and economic shock, as it was a largely unexpected shock.

The UK's exit from the EU also shocked the European society. Many companies' managers have stated that Brexit created a turning point and was more like a shock, regardless of whether it would have negative or positive effects. The turning point began when they started talking about it until the referendum in 2016 and then the UK's exit in 2020. It was an unusual event for the European community, especially for UK companies where they faced this scenario for the first time. Furthermore, such political exits increase the pressure on the financial markets, banks, and all economic sectors. The subject has also been a matter of controversy and debate among the British themselves, as it took about four years to get out of the EU, while the UK was hoping to get out with minimal losses and to make all Britons accept this new reality (Aldrick, 2022).

Brexit will lead to a major structural change in the financial structure of the UK in the coming years. It will affect investment activities, banking activities, derivatives trading, financial policies, and financial markets. UK companies rely on providing services in these areas, and the provision of these services is currently linked to the nature of the legislation and laws that will be agreed upon by the EU and the UK. It is difficult to predict the exact impact of Brexit on the future financial structure of the UK at this stage, as there is a possibility that this impact will change over time. The EU and the UK should be prepared for all scenarios, including regulatory and supervisory divergences where considerations of financial stability or lack thereof will be a major factor in upcoming decisions (Bergbauer et al., 2020).

So, to what extent the UK's exit from the EU will affect the capital structure of the firms? How will these firms deal with this issue, and how will these companies face this situation, being still concerned about what they will face in the coming period regarding the laws and regulations discussed between the UK and the EU? Also, what will be the financial laws and regulations that will be agreed upon between the two parties and the impact of these political decisions on the performance of the UK companies?

The paper addresses the impacts of the political exits on the capital structure policies, taking the impact of the Brexit deal on UK companies as a practical case. The paper sheds light on Brexit's political risk and uncertainty and links it directly to the capital structure policies of the UK firms listed in the FTSE 100 over 12 years. In addition, the study aims to confirm the interaction between political decisions and capital structure, even in countries that enjoy political and economic stability. Political exit could be a shock for companies working there and may lead to increased uncertainty. Therefore, companies seek to adopt new procedures or measures for changing their financial policies to mitigate the impact of this shock and adapt faster to these changes.

The study could be useful for academics specializing in finance and economics, as the paper shows the impacts of political exits on capital structure policies, taking the Brexit deal and its impact on the UK's companies as an example. Moreover, this study could be helpful for EU members and the UK government, taking into consideration the interests of the UK and EU where any future policies or laws will affect the financial and economic sectors of the two parties.

Literature Review

Politics is related to the economic and financial policy of any country, where the impact of political decisions and practices is reflected in economic and financial trends. O'Leary (1985) states that political concept in societies is directly related to how the government carries out and implements its political activities on the ground. However, sometimes it may be used incorrectly when applied to theory and practice. Therefore, the link between the political system with the corporate financial policies must be recognized as a key factor in ensuring the development of companies and maintaining their continuity. The current political climate is imposing new conditions on the global stage, as more regulations and practices were observed to control markets in order to play a major role in corporate governance. These procedures affect the financing of banks, insurance companies, and other companies (Jensen, 1991).

Political factors are an important metric while constructing the capital structure policy because of their influence and connection with it. Myers (2009) mentions that political decisions, or rather the performance of politicians, influence capital structure policies in different ways. For example, when companies face political pressure or forced to abide by a political law or governmental decisions, companies seek to improve their debt levels with the aim of discouraging politicians from doing so. This increases the potential for financial distress with leverage, as firms increase their debt optimally to discourage costs from hostile politicians. In contrast, when friendly politicians issue facilitating decisions or encouraging laws for companies, the companies will optimally reduce their debt levels.

Political instability has a lot of impacts on capital structure policies. Thus, Holmen and Pramborg (2009) analyzed the impact of the political risks on a firm's capital structure policies. They found that in the presence of capital market deficient, unsystematic, and country-specific political risks, capital structure policies are affected. Political risk pushes managers to take these risks into consideration and to study different options while developing their capital structure policy. Moreover, Cao et al. (2013) examine the role of political uncertainty in

capital structure decisions where the results show that leverage ratios are negatively related to political uncertainty. However, firms that have access to public debt markets are less sensitive to changes in political uncertainty when determining capital structures.

In addition, political risks or uncertainty greatly affect the capital structure policies in many cases. Thus, Waisman et al. (2015) brought new empirical evidence that political uncertainty is associated with higher corporate debt financing costs. The characteristics of corporate bonds that could affect the firm's cost of debt financing are related to the uncertainty associated with the outcome of the US presidential election. It leads to a 34-basis point increase in corporate bond spreads, with closer campaign years associated with additional costs. Furthermore, Joong Im et al. (2020) investigated how political uncertainty affects firms' capital structure using a panel data set of U.S. public firms between 2003 and 2018, where they found that high uncertainty firms have 10% points lower mean book (market) targets than low-uncertainty firms.

Exits from political unions, such as the Brexit case, could be a challenging and shocking step for the UK companies. Managers have to deal with new changes in their surrounding environment and start embracing these changes, even by updating or changing their capital structure policies. For example, DeAngelo (2007) mentions that managers developing corporate financial policies face a challenging and competitive environment the whole time. In every decision-making, managers must understand the impacts of today's decisions on the set of possible choices in the future. Therefore, financial policy decisions include all variables of the basic financing model for investment in real assets, investment in financial assets, capital infusions from debt and equity issuance, and recapitalizations.

Many studies were conducted about capital structure policies, where researchers investigate the key factors and variables that affect the capital structure, and its determinants. Our study sheds light on the impact of the political exits on capital structure policies. Therefore, it is important to focus on some previous studies that investigated the impacts of political factors on the capital structure (such as Fraser et al., 2006; Myers, 2009; Liang et al., 2022 etc.). Mainly, the paper depends on the studies that analyze the relationship between political factors and the capital structure, by addressing the impacts of political decision and practices on the capital structure policies.

There are many variables that could be used to study the capital structure decision and practices, such as leverage, debt ratio, profitability, tangibility, liquidity, size, tax paid, propensity to pay dividends, growth, profit, and non-debt tax shield, etc. However, this study depends mainly on the shared variables and indicators that were used in the studies listed below in Table 1, because of their importance for analyzing capital structure policies. Of course, some indicators were ignored, as it is not possible to study all of them at the same time. But it is mentioned below variables among all others that play an important role in our study. Table 1 shows the capital structure determinants chosen for our study.

Many factors play a key role while developing the capital structure policies. For example, managers take into consideration internal and external factors within the company, such as cost of capital, business size, government policies, competition, taxation policy, degree of control, flexibility of financial plan and business nature (Sangeetha, & Sivathaasan, 2013). Capital structure requires several tactics to make the right decision, as it tackle complex and emergency situations. For Muneer and Rehman (2012), decision-making is a cognitive process of choosing an alternative from among many possible alternatives. Capital structure is usually being managed with a two major theories trade-off theory and pecking order theory.

Table 1

Indicators, Proxy, Variable Type and Related Studies for the Capital Structure Determinants

Indicator	Proxy	Variable Type	Studies
LTD/TE	Long term Debt / Total Equity	Dependent	Lourenço and Oliveira (2017); Dermeval et al. (2017); Loan et al. (2016); Dragotă et al. (2018); Devos et al. (2017)
Profitability	Net Income / Total Asset	Independent	Dermeval et al. (2017); Lourenço and Oliveira (2017); Loan et al. (2016)
Tangibility	Fixed Assets / Total Asset	Independent	Dermeval et al. (2017); Lourenço and Oliveira (2017); Loan et al. (2016); Harc (2015)
Liquidity	Current Asset / Current Liability	Independent	Lourenço and Oliveira (2017; Loan et al. (2016); Dermeval et al. (2017)
Propensity to pay dividends (dummy)	payer / non-payer	Independent	Mohsin (2016); Krištofík et al. (2022); Jiang et al. (2017); Zou and Bai (2022)
Size	Natural Log (Total Assets)	Independent	Lourenço and Oliveira (2017); Loan et al. (2016); Dermeval et al. (2017)
Political factor (dummy)	Political events and news	Independent	Lourenço and Oliveira (2017); Mohsin (2016); Kesternich and Schnitzer (2010)

Source: Compiled by the author.

Developing a capital structure policy within a complex political condition considered as a challenge for the companies. Brexit was creating a shock and a state of uncertainty for UK companies, which promotes board of directors and managers to develop a capital structure policy that can adopt with the surrounding circumstances. Managers can benefit from the two major theories such as trade-off theory and pecking order theory while developing their capital structure policies. For example, trade-off theory depends on the leverage to construct capital structure by assuming leverage-benefits (Modigliani, & Miller, 1958), while pecking order theory depend on the internal financing, where it focuses on its internally generated sources such as retained earnings to finance firm operations (Myers, & Majluf, 1984).

Tested Hypothesis

There are some researchers who believe that political practices and decisions have no impact or even a weak impact on the corporate financial policy, especially on the capital structure. They believe that these issues are internal issues decided by the BOD and managers of each company. For example, Asquer and Calderoni (2011) mention that political connections are not associated with company's policies where political connections cannot guarantee positive companies returns where maintaining a connection with the Politicians may has no effect, or even a negative effect on the companies' performance. Moreover, Feltri et al. (2017) stated that finance researchers did not pay much attention to political economy until the impact of politics on the economic and financial sectors began to emerge until the past two decades. This theory [H0] is adopted by some authors, who believe that politics charts the general framework of the financial policies, but it does not interfere in the capital structure policies. These issues are an internal matter for corporations, decided usually by the BOD, managers and stakeholders, who draw the company orientation and determine the financial policies.

H0: The exits from political unions have no impact on the capital structure policies.

On the other hand, there are other researchers who investigate about the relation between politics and corporate financial policies, where they consider that politics and financial policies are correlated to each other. Politics have a direct impact on the companies' performance, and their capital structure decision. For example, Julio and Yook (2012) mention that politics often stand behind the decisions that cannot be predicted and create a state of uncertainty and instability especially when talking about incentives and uncertainties associated with

possible changes in government or national leadership policy that have implications on the company's performance and their financial policies. In addition, Fisman (2001), and Allen et al. (2005) argues that political connections help companies to obtain an advantage in building their financial policies when firms connected to the government. Furthermore, Myers (2009) mention that the political environment in which the company operates affects the capital structure of the company. So, the political atmosphere may create a state of uncertainty and the political instability could affect the firm's capital structure. The below hypothesis [H1] was adopted by many researchers who believe that political decisions such as the exit from the political unions have a lot of consequences on the capital structure policies.

H1: The exits from political unions change the capital structure policies.

Methodology

The study depends on financial indicators and variables collected from UK companies listed at FTSE 100 between the period (2010-2021), before and after the Brexit deal (2016). Data were collected from the annual reports of the companies from their official websites and from FTSE 100 data base. Brexit negotiations start at 2016, and in order to analyze the impact of Brexit deal on the UK companies, selecting a period of 12 years (6 years before, and 6 years after). The first period was between 2010 & 2015, while the second was from 2016 till 2021.

Moreover, capital structure policies were studied through studying the determinants of capital structure. A regression analysis was adopted to interpret the variables, using a multiple linear regression. The paper also studies how much the political exit affecting the variables and how did they change by applying of dummy variable to study the impact of political factor "Brexit" on the capital structure determinants.

The determinants of the capital structure that used in the study are as follows: LTD/TE, profitability, tangibility, liquidity, propensity to pay dividends (dummy), size, political Factor—Brexit (dummy). Several studies about capital structure used LTD/TE as dependent variable such as D'Mello et al. (2018), Devos et al. (2017), and Demirgüç-Kunt et al. (2020).

For measuring LTD/TE, dividing long term debt over total equity. Profitability is measured by dividing net income over total asset. Moreover, tangibility is measured by dividing fixed asset over total asset. Liquidity is measured by dividing current asset over current liability. Propensity to pay dividends (dummy) determined as payer or non-payer. Size is scaled through natural log of total assets. Finally, political factors (dummy) represented by Brexit is scaled through political related events and negotiations.

During data collection, some abnormal values and missing values of indicators appear, but our statistical programs eliminate such cases, the percentage of missing data is low in our case. Regarding survivorship bias, a very selective data resources was chosen where it does not omit observations that are no longer in existence, where we check if the companies' list from FTSE 100 index is still the same in the end of the analyzed period. Only two companies were reshuffle from the index but their financial data were inserted within the study. In addition, some cases observed in which a company recorded losses especially in profitability, where the values were inserted in negative sign and the SPSS software process it.

The study contains panel data and time series format which includes both cross section and time dimension, so, it is better to adopt regression as econometric analysis. Therefore, empirical expression of the main model in Table 1 is expressed as in equation (1).

$$LTD/TE_{it} = \beta_0 + \beta_1 Prof_{it} + \beta_2 Tan_{it} + \beta_3 Liq_{it} + \beta_4 Sz_{it} + \beta_5 PTPD_t + \beta_6 PF_t + \varepsilon_{it} \quad (1)$$

where LTD/TE is long term debt over total equity, Prof is profitability, Tan is Tangibility, Liq is Liquidity, Sz is

Size, PTPD is propensity to pay dividends, PF is political factor.

According to Eq. 1 above, the dependent variable is the long-term debt over total equity (LTD/TE), where profitability, tangibility, liquidity, size, propensity to pay dividends, and political factor are the independent variables, i represent each company; t represents the year; and β0 represent the constant coefficient where β1, β2, β3, β4, β5 & β6 represents the coefficients of the independent variables. However, propensity to pay dividends and political factor are a dummy variable where the propensity to pay dividends will have scaled through two choices (payer/non-payer) while the political factor is represented by Brexit deal and its related events. "PTPD" is a dummy variable that takes the value 1 in the case of paying dividends and 0 for non-payer. "PF" is a dummy variable that takes the value 1 in the case of existence of Brexit related event and 0 otherwise.

Moreover, the referendum for Brexit was start at June 2016 which means that before this date there was no direct impact for Brexit on the corporate financial policies for UK companies. However, after the referendum a lot of negotiations and discussions were happened between the two parties to reach a final agreement until the beginning of 2020 where Brexit is taken place. During these periods (2016-2021) a lot of negotiations or events were happened between the two parties "UK & EU" which leads finally to the split of UK from the EU at Feb. 2020. These events and factors effects on the corporate financial policies for UK companies. The aim of the study is to shed light to which extent the political factor represented by Brexit affecting on the capital structure policy.

Many studies used the same methodology in studying capital structure such as Orlova et al. (2020), Klasa et al. (2018), and Ha et al. (2018) etc. In addition, some studies who depend on political factors, political events and news to analyze the corporate financial policies such as Holmen and Pramborg (2009), and Brunzell et al. (2013), where they analyze the impact of political factors such political risk and uncertainty to determine the impact of political factors on the corporate financial policies and companies' performance. The data collected method is aligned with previous studies such as Kinneging (2020), and Kaya et al. (2018), where these studies collect their data depending on the annual reports of the UK firms listed in FTSE 100 and study the impact of Brexit on the investment decision and capital structure. Previous studies included regression analysis and empirical tests about the capital structure determinants. Indeed, the paper follow the same strategy.

However, the important factor in this methodology was to study the impact of the political factor represented by Brexit on capital structure policy for UK firms listed at FTSE 100, during the period (2010-2021). It was important to show the impact of the political factors such as political decisions, practices, governmental regulations and laws on the determinants of the capital structure policies.

Results

The Brexit negotiations between UK and EU were leaving its impacts on the UK companies' and their performance. The findings show that the financial ratios were differed between the two periods (before and after) Brexit. The SPSS software was adopted to analyze and interpret the variables to reach our results as shown below.

Table 2 below provides summary statistics for the main variables of UK firms listed at FTSE 100. To minimize the effect of outliers and extreme values, we winsorize all ratio variables at the 5th and 95th percentiles of their distributions. The differences between ratios for capital structure determinants are statistically significant, where long term debt over total equity decreased from a mean value of 0.68 to 0.63 after the referendum. In addition, profitability was decreased from 0.10 to 0.08, and tangibility were also decreased from 0.49 to 0.46. However, liquidity was increased from 1.45 to 1.56 after the referendum, also size was increased from 4.10 to 4.31 during Brexit.

Table 2

Descriptive Statistics

Period [2010-2015]	Mean	Median	Std. Dev.	Variance	Skewness	Kurtosis	Range	Min	Max
LTD/TE	0.686	0.390	1.157	1.339	2.23	5.820	4.091	0.157	4.241
Profitability	0.101	0.055	0.223	0.05	3.313	4.125	2.294	-0.18	2.474
Tangibility	0.491	0.433	0.743	0.553	4.683	4.284	0.642	0.312	0.903
Liquidity	1.455	1.208	1.090	1.189	1.909	3.894	6.615	0.012	6.627
Size	4.101	3.981	0.953	0.909	0.481	-0.026	4.702	1.881	6.583
Paying Dividends	0.966	1	0.206	0.042	-3.449	4.854	1	0	1
Political Factor	0.402	0.5	0.341	0.116	-	-	1	0	1
Period [2016-2021]	Mean	Median	Std. Dev.	Variance	Skewness	Kurtosis	Range	Min	Max
LTD/TE	0.632	0.376	0.974	0.948	1.849	5.512	4.184	0.184	4.382
Profitability	0.086	0.048	0.205	0.042	5.646	4.213	2.058	-0.26	2.318
Tangibility	0.465	0.386	0.636	0.404	4.492	3.878	0.517	0.412	0.931
Liquidity	1.561	1.204	1.195	1.427	1.732	3.324	6.646	0.018	6.664
Size	4.314	4.085	0.892	0.796	0.736	0.15	4.492	2.471	6.963
Paying Dividends	0.919	1	0.257	0.066	-3.358	4.307	1	0	1
Political Factor	0.651	0.5	0.308	0.095	-	-	1	0	1

* measurement unit: ratio / currency in (£m)

Source: Compiled by the author.

Notes: LTD/TE = long term debt over total equity, Std. Dev = Standard Deviation, Min = Minimum, Max = Maximum.

Depending on the descriptive statistics in Table 3, the figures below show the variation of variables before and after Brexit during the period (2010-2021).

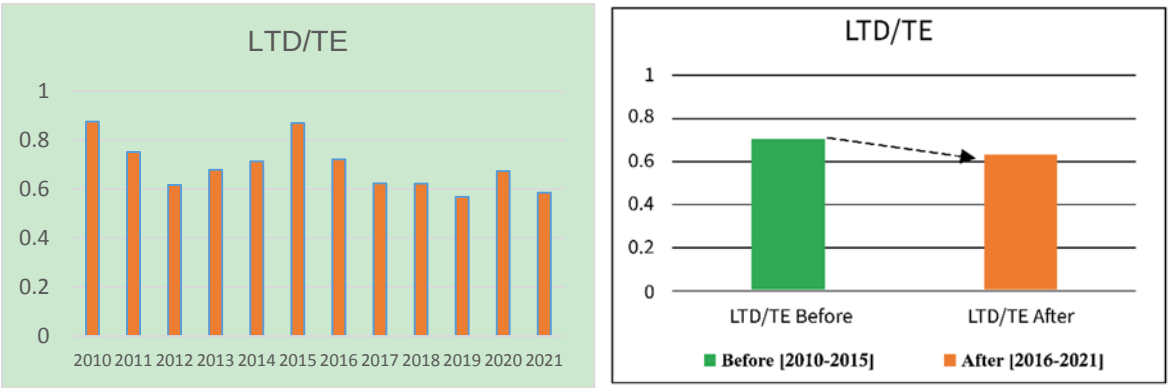

Figure 1. Variation of LTD/TE during the period (2010-2021).

Source: Compiled by the author.

Figure 1 shows that LTD/TE was decreased by 7.8%. This ratio used to evaluate the company's financial leverage where it measures the degree to which extent a firm is financing its operations with debt rather than its own resources. A lower ratio means that the UK companies is decreasing their debt, which is a sign of a financially responsible companies with a steady revenue stream in order to stay in a safe position during uncertainty and vague political atmosphere during Brexit. Large companies listed in FTSE 100 have more than 40% of long-term debt to equity. The results aligned with the results of other studies such as Hatzinikolaou et al. (2020), and Im et al. (2020).

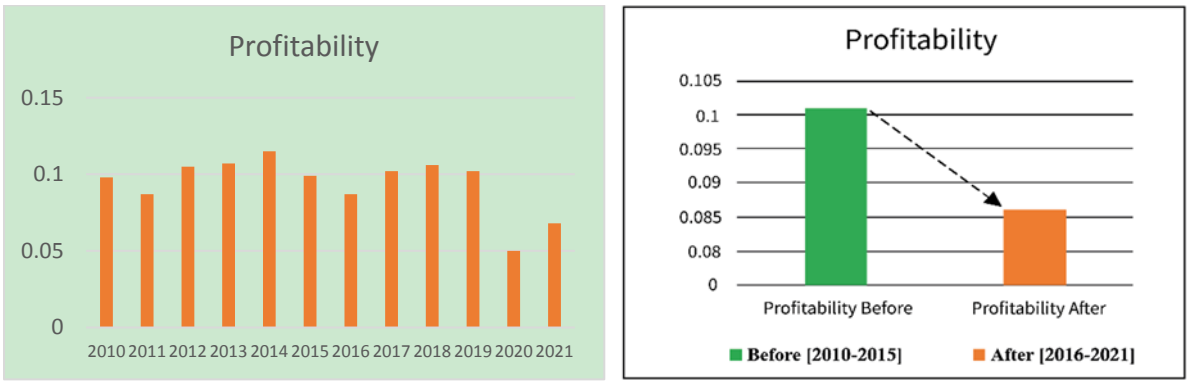

Figure 2. Variation of profitability during the period (2010-2021).
Source: Compiled by the author.

Moreover, profitability was decreased by 14.8%. It seems that UK's exit from the EU contributed to loss its part from EU markets. So, UK companies must find alternative markets and expand outside EU to find additional markets. In addition, uncertainty and political risk affect the companies' profitability and their overall return in many ways (Dang, & Nguyen, 2022; Athari, 2020). Moreover, the results reveal significantly negative relation between debt and profitability (Shubita, & Alsawalhah, 2012). A similar study about capital structure and profitability at UK show that the firm's capital structure has a significant influence on the profitability of SMEs in the UK (Yapa Abeywardhana, 2016).

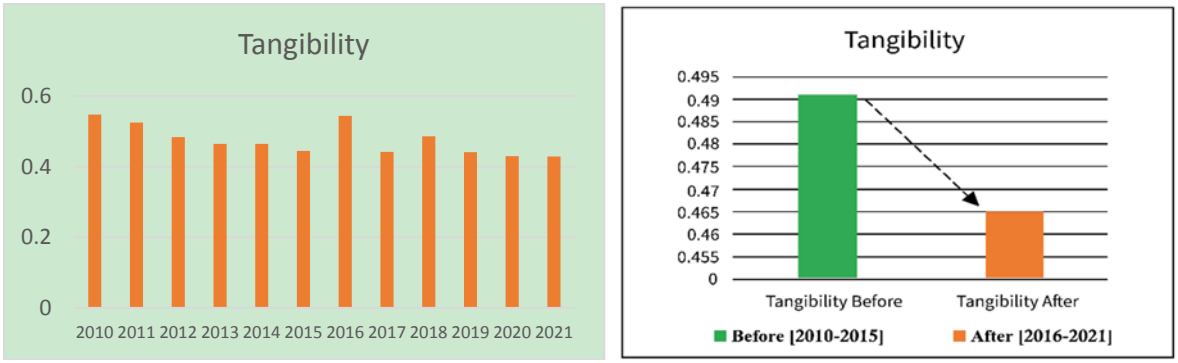

Figure 3. Variation of tangibility during the period (2010-2021).
Source: Compiled by the author.

In addition, tangibility was decreased by 5.9%. Regarding the UK case, it seems that the UK companies show its dependence on the debt financing in order to run its business. Similar results were reached such as Favara et al. (2021), and Kim (2018) regarding political risks and tangibility. A high ratio of tangibility could allow the firm to obtain external financing easily resulting in a high leverage (Arilyn, 2019). Investors consider tangible assets as part of total assets as a positive measure, and extending the debt level in this case is quite normal (Serghiescu, & Văidean, 2014).

Figure 4. Variation of paying dividends during the period (2010-2021).
Source: Compiled by the author.

Propensity to pay dividends was decreased by 4.9%. This reflects the logical pattern for the UK firms during the uncertainty of Brexit negotiations. For example, Chay and Suh (2009) find that risk negatively impacts both the probability of paying dividends and the amount paid. Also, Huang et al. (2015) provide international evidence that political risk bears negatively on dividends, where Bliss et al. (2015) show that the 2008-2009 financial crisis was led to decrease in corporate payout.

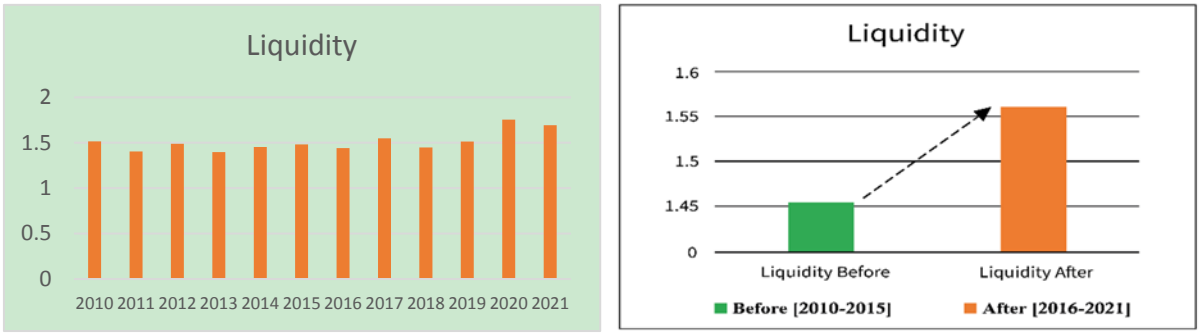

Figure 5. Variation of Liquidity during the period (2010-2021).
Source: Compiled by the author.

On the other side, Liquidity was increased by 7.3%. UK companies trying to stay in safe financial position and preventing to face financial hardships. The higher ratio belongs to the safety margin that the business possesses to meet its current liabilities. Baum et al. (2011) found that liquidity is sensitive to political risks and uncertainty. Liquidity crises are closely related to the impact of uncertainty on the optimal portfolio (Routledge, & Zin, 2009). Firms with relatively predictable liquidity have the ability to anticipate the likely trading costs associated with transacting.

Firm size has become a main control variable in empirical corporate finance studies where firm size has been empirically found to be strongly positively related to capital structure (Kurshev, & Strebulaev, 2015). Here, size was increased by 12.5% where it seems that the UK companies are expanding and benefiting from all their resources especially after Brexit, where many managers believe that Brexit will create a chance for their companies to expand to another countries and markets in different regions of the world. Indeed, large firms tend to have higher leverage ratios than small firms in order to invest more and increase their profitability (Unal et al., 2017).

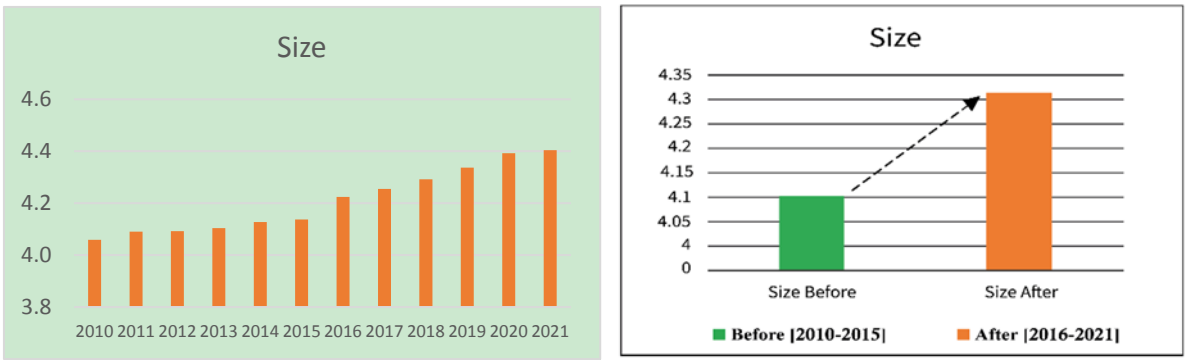

Figure 6. Variation of firm size during the period (2010-2021).
Source: Compiled by the author.

The correlation matrix in Table 3 below shows that LTD/TE has a negative linear correlation with profitability and liquidity, where LTD/TE has a positive linear correlation with tangibility, size, and paying dividends. The results show that the Brexit negotiations have an impact on the capital structure determinants and variables by a magnitude impact of 13.7% on capital structure variables. Usually, the political uncertainty or risk play a key role in changing financial policies, where previous studies such as Waisman et al. (2015), and DeBenedetti (2014) found a direct relation between the political factors and the corporate financial policies which assure our results.

Table 3
Correlations

	LTD/TE	Profitability	Tangibility	Liquidity	Size	Political Factor	Paying Dividends
LTD/TE	1						
Profitability	-0.058* (0.049)	1					
Tangibility	0.064* (0.030)	0.004 (0.891)	1				
Liquidity	-0.171** (0.000)	0.021 (0.471)	-0.008 (0.789)	1			
Size	0.008 (0.786)	-0.107** (0.000)	-0.160** (0.000)	-0.114** (0.000)	1		
Political Factor	-0.072* (0.014)	-0.035 (0.234)	-0.021 (0.469)	0.046 (0.114)	0.114** (0.000)	1	
Paying Dividends	0.027 (0.363)	0.054 (0.066)	-0.005 (0.861)	-0.078** (0.008)	-0.023 (0.438)	-0.057 (0.053)	1

*. Correlation is significant at the 0.05 level (2-tailed).
**. Correlation is significant at the 0.01 level (2-tailed).

Source: Compiled by the author.
Notes: LTD/TE = long term debt over total equity.

In addition, our results were aligned with the results of ALmuaither and Marzouk (2020). The UK firms depend on two main theories, trade off and pecking order theory among capital structure theories, according to their procedures and techniques they follow. The political atmosphere is playing a key role while UK companies developing their capital structure policies and building their decisions regarding financing from debt or equity in order to make a balance between them or employing internal fund such as retained earnings during economic recession.

Table 4

Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	0.30a	0.41	0.36	1.13405

a. Dependent Variable: LTD/TE
b. Predictors: (Constant), Paying Dividends, Tangibility, Profitability, Liquidity, Size

Source: Compiled by the author.

Notes: LTD/TE = long term debt over total equity, R = correlation coefficient, R Square = coefficient of determination, Adjusted R Square = adjusts R Square for the number of predictors in the model.

Based on the above results, Table 4 shows that R equals to 0.30 where the value of R-squared is equals to 0.41 which means that 41% of the variation in the independent variables are explained by the dependent variable. In addition, the Adjusted R-squared equals to 0.36 which is significant in the regression model.

Table 5

Significant Test

Model	Sum of Squares	df	Mean Square	F	Sig.
Regression	53.792	6	8.965	8.125	0.000b
Residual	1272.202	1153	1.103		
Total	1325.994	1159			

a. Dependent Variable: LTD/TE
b. Predictors: (Constant), Paying Dividends, Tangibility, Profitability, Political Factor, Liquidity, Size

Source: Compiled by the author.

Notes: df = degrees of freedom, F = F-value, Sig = Statistical Significance.

Moreover, Table 5 shows the regression analysis results where the F-value equals to 8.125 which is greater than p-value that equals to $\alpha = 0.000 < 0.05$ which means that there is a low probability that H0 is true, so reject H0. The data are statistically significant which means that our results likely did not happen by coincidence, so the null hypothesis can be rejected.

H0: not significant; H1: significant.

Table 6

Fixed Effects

Model	Unstandardized Coeff.		Standardized Coeff.	t	Sig.
	B	Std. Error	Beta		
(Constant)	0.931	0.211		4.412	0
Profitability	-0.287	0.145	-0.057	-1.977	0.048
Tangibility	0.095	0.045	0.061	2.1	0.036
Liquidity	-0.155	0.027	-0.166	-5.67	0.000
Size	0.000	0.034	0.000	0.012	0.491
Political Factor	-0.137	0.062	-0.064	-2.202	0.028
Paying Dividends	0.063	0.133	0.014	0.47	0.538

*Dependent Variable: LTD/TE

Source: Compiled by the author.

Notes: LTD/TE = long term debt over total equity, t = t-statistic, B = Beta, Std. Error = Standard Error, Sig = Statistical Significance.

Table 6 shows beta for each variable in addition to the statistical significance for the capital structure determinants. Our results were aligned with previous studies regarding the impact of political factors, risk and

uncertainty on the capital structure policies. For example, Ben Ameur and Louhichi (2022) investigate the impact of Brexit on the European financial markets, where the results show that between Sept. 2015 and Sept. 2016, the high level of volatility confirms the strong degree of market integration, with uncertainty surrounding the referendum outcome having a clear impact on the main European markets. Furthermore, our results were aligned with the results of Sezgin and Bayar (2021), where Brexit deal has the potential to affect the stock markets through enhancing the risk and uncertainty. They study the impact of Brexit on the UK stock markets over the period between May 2016 and May 2021 by depending on empirical analysis. The results indicated that emergence and finalization of Brexit caused the structural changes in the course of stock market index. Our main objective was to find a direct relation between the political factor and the capital structure policies for UK companies listed at FTSE 100 index. Indeed, a direct relation between them were founded as Sezgin and Bayar (2021) considered that Brexit has an impact on the FTSE 100 index.

Conclusions

The paper examines the impact of political exits, particularly Brexit, on the capital structure policies of UK companies listed at FTSE 100. It argues that political decisions, such as exiting from political unions, can significantly influence financial policies and company performance, creating uncertainty that forces businesses to adapt or change their financial strategies. The study highlights the historical link between political practices and financial policies, and explores how political uncertainty—generated by Brexit—affects corporate financial decisions.

In addition, the paper shed light on the political risk and uncertainty of Brexit and linked it directly to the policy of the capital structure at the UK over 12 years. The study examines the firm's specific determinants of capital structure for 100 UK companies during the period 2010-2021. The data obtained from the annual reports of the UK companies and from FTSE 100 data base.

The results show that the financial ratios were differed before and after Brexit, where the capital structure determinants and variables were affected starting from 2016 due to Brexit referendum and then the political negotiations, and then the Brexit deal between the two parties during the period (2016-2021). Moreover, the correlation matrix shows that LTD/TE has a negative linear correlation with profitability, liquidity, and political factors where it seems that LTD/TE has a positive linear correlation with tangibility, size, and paying dividends.

Moreover, the analysis of UK companies' financial variables reveals several key trends. The debt-to-equity ratio (LTD/TE) decreased by 7.8%, indicating that UK firms reduced their reliance on debt, likely in response to the political uncertainty surrounding Brexit. Profitability dropped by 14.8%, reflecting the loss of access to EU markets and the impact of political risk on returns. Tangibility decreased by 5.9%, suggesting that companies were less able to leverage physical assets for debt. The propensity to pay dividends also fell by 4.9%, consistent with the negative effect of risk on dividend payouts. However, liquidity increased by 7.3%, as companies sought to maintain a safer financial position amidst uncertainty. Additionally, firm size grew by 12.5%, as larger UK firms expanded to new markets outside the EU. These findings align with studies on political risk and financial strategies, showing how Brexit's uncertainty influenced UK companies to adapt their financial policies in order to navigate the challenges.

Developing capital structure policies involves considering internal and external factors such as cost of capital, business size, taxation, and government policies. Managers often rely on trade-off theory and pecking order theory to guide decision-making. In complex political conditions like Brexit, uncertainty forces UK

companies to adapt their capital structure strategies. The trade-off theory focuses on balancing debt and equity to maximize benefits, while the pecking order theory prioritizes internal financing, such as retained earnings. Both theories help managers navigate challenges and make informed decisions about financing.

It's clear that the political atmosphere leave it's impacts on the capital structure policies for the UK companies. During the whole period of negotiations between UK and EU, where a direct impact of political atmosphere was noticed on the capital structure policies for UK companies. So, according to the previous results we can conclude that the results reject H0 and supports H1 hypothesis, which assure that the exits from political unions change the capital structure policies.

The paper has two main limitations. First, the studied period for the impacts of Brexit on capital structure policies consists of 6 years (2016-2021), perhaps if the study period was longer, it would have come out with more accurate results. Second, there were many factors that could be studied, but due to our timeline and our schedule, the most influential factors in the study were choosed.

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