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RESEARCH PAPER

The Role of Financial Flexibility in the Financial Performance of the Automobile Sector: Asian Perspective

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ABSTRACT

In the corporate sector, financial managers emphasize the importance of Financial Flexibility in the company's financial operations which enables the company to navigate uncertainties effectively. The purpose of this study is to examine the role of financial flexibility in the financial Performance of the automobile sector Asian perspective from 2013 to 2022. Three different measures of financial flexibility were used in this study net cash flows, market capitalization, and degree of financial leverage. This study used the two-step system Generalized Method of Moments (GMM) dynamic panel estimator for empirical testing of the hypothesis by using secondary data from 19 listed automobile companies to investigate the performance of firms. The results of this study show that the degree of financial leverage significantly negative impact on Investment activities and Tobin Q along with the background theories like Trade-off theory and Theory of investment and there is a positive impact of the degree of financial leverage on return on assets. This study recommends that policymakers and corporate managers seek to reduce the risk of financial distress and improve financial performance.

KEYWORDS Debt Levels, Financial Flexibility, Financial Performance, Market Capitalization, Net Cash Flows

Introduction

The In the current global economic conditions, companies are more competitive, which forces them to actively pursue strategies that will secure their survival and improve the overall performance of the firms to meet their company objectives. The primary objective of any company is to maximize profits through the identification and capitalization of superior investment opportunities, thereby improving overall financial performance (Ahmad et al., 2023). Putri and Willim (2023) stated that a company's capital structure plays an essential part in determining its financial health as it has a direct impact on its financial position.

Financially flexible firms strategically maintain a reserve of borrowing power which gives them the flexibility to react quickly to unexpected circumstances and capture future growth opportunities (Raza et al., 2021). This financial flexibility enhances a company's resilience, and adaptability by managing the changing business environment, and opt profitable investment opportunities (Islam et al., 2020). The importance of financial flexibility in the context of corporate management is demonstrated by the common agreement of senior corporate managers, who view it as a critical factor in guiding their capital structure decisions.

Corporate chief financial officers always place a high priority on financial flexibility because they see it as the main goal that drives their financial policies and decisions (Tripathi et al., 2018). Financial flexibility is consistent with the primary objective of corporate finance which is to avoid expensive financial hardship, reduce the danger of underinvestment, particularly during difficult times, and facilitating the sort of strategic decision-making that fosters resilience and long-term success (Agrawal, 2020).

Businesses have traditionally concentrated on achieving stability through competent financial practices. However, as the corporate environment has evolved, there has been an increasing demand for financial flexibility. Moreover, the accessibility of financial resources becomes crucial for navigating through the difficulties caused by complex market dynamics. Therefore, financial flexibility emerges as a critical element that contributes positively to financial performance (Ali & Siddiqui, 2020).

Financial flexibility is the company's capability to manage a substantial pool of untapped borrowing options. This strength is observed when firms can obtain funds when needed, reducing the chance of default payment. Furthermore, having the ability to receive funds quickly gives businesses more financial flexibility because it makes it possible for them to handle unforeseen events without compromising their stability. The surplus cash reserves play a crucial role in improving economic flexibility for publicly traded companies because they serve as a hedge against future financial and insurance difficulties (Islam et al., 2022).

Financially flexible firms possess the ability to access and restructure their funding at a low cost by having a stable financial situation which is essential for resolving underfunding problems, especially when resources are limited, and having financial flexibility which helps to avoid the expenses that come with unfavorable circumstances (Zhang et al., 2020).

The performance of a company serves as a comprehensive measure of its overall effectiveness, taking into consideration both financial and operational aspects. The success of a firm is largely attributed to its performance over a specific period, which reflects its ability to achieve desired outcomes (Hermuningsih et al., 2020; Sahoo, 2021). Additionally, a well-established corporate management system plays a crucial role in attracting investment by maximizing the company's resources and strengthening its foundation which in turn, leads to the expected enhancement of firm performance. Moreover, the process of developing a strategy is crucial to strategic management because it largely determines a firm's ability to achieve its strategic objectives (Selvam et al., 2016).

Financial flexibility is particularly important in corporate financing decisions in developing countries because organizations with greater financial flexibility are more resistant to negative external shocks than their less flexible counterparts (Chen et al., 2017; Mahmood et al., 2022). Financial flexibility empowers companies to navigate their capital structure with greater efficiency, offering a range of strategic advantages (Chen et al., 2017). Some companies opt to maintain substantial cash reserves to buffer against unforeseen circumstances, enhancing their ability to overcome their risk of debt, and thereby strengthening their financial resilience (Mahmood et al., 2018).

There are many studies have been done on financial flexibility in different sectors but not a single research has been done on the role of financial flexibility in the financial performance related to the automobile sector from an Asian perspective. This study expanded the theoretical scope of financial flexibility which impacted the financial performance by contributing to the existing literature. Moreover, this study also contributes to the existing literature with the empirical evidence that the return on assets is positively correlated with the degree of financial leverage which indicates that firms with higher levels of debts are more likely to generate profits on return by utilizing debts in financing projects.

Financial Flexibility in Pakistan

Financial flexibility plays a critical role in shaping overall financial performance, particularly in developing countries such as Pakistan. Financial flexibility is essential for corporate firms but it depends on two things: having the right goals and being able to achieve and maintain them. This flexibility enables firms to adapt to changing economic conditions, and navigate challenges effectively. Furthermore, it is important for industry participants

and the economy as a whole in the context of Pakistan's automobile sector. Pakistan's automotive industry experienced a substantial decrease in demand from the duration of the financial year spanning from 1st July 2022 to 30th June 2023. The significant downturn in sales can be attributed to various factors, including economic challenges, fluctuating consumer confidence, and perhaps disruptions caused by the global pandemic (Rehmat et al., 2023). Figure 1.1 shows the volume and growth of Honda Atlas Cars (HCAR) and Indus Motor Company (INDU) witnessed the most substantial declines in volumes, dropping by 63% and 57% year on year, respectively. However, looking ahead to fiscal year 2021, there's an optimistic outlook, with expectations of a significant rebound in volumes.

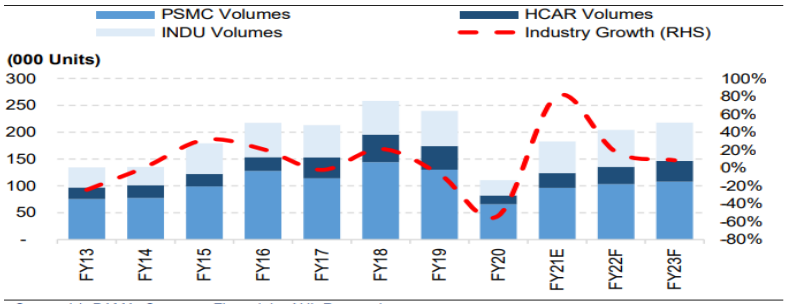

Figure 1. Automobile assemblers' volume and growth, Source: PAMA, Company Financials, AHL Research

There are several studies have examined on financial flexibility across various industries in developed countries and developing economies but have not found any research on the relationship between financial flexibility and financial performance in the automobile sector (assemblers + spare parts) Asian perspective.

This study attempts to analyze the general objective of the role of financial flexibility in the financial performance of the automobile sector from an Asian perspective.

Literature Review

Financial flexibility refers to a firm's ability to boost its internal resources. When a company has good financial flexibility, it can increase its investments and take advantage of beneficial opportunities. Choudhry and Mizerka (2018) stated that financial flexibility is found to be essential for firms and serves as a valuable asset in their operations. Financially flexible firms tend to function better and more steadily than those that are not financially flexible.

Financial flexibility is a company's capability to effectively adapt to unforeseen changes in cash flows or investment options. Essentially, financial flexibility involves obtaining the required funds to fulfill specific functions at the lowest possible cost (Al-Slehat, 2019). Financial flexibility is seen as a positive attribute for companies because it has the potential to enhance both growth and financial performance (Ridha & Takarini, 2024). The financially flexible firm can efficiently manage its finances and adapt strategies to maximize its overall worth (Altaf, 2020; Raza et al., 2021).

Financial flexibility becomes essential because it enables the management of a company to take on potentially risky projects, even when the market is disrupted. Due to their flexibility, they can pursue profitable agreements and overcome obstacles (Agarwal et al., 2020; Settembre-Blundo et al., 2021). Financial flexibility is a crucial factor that empowers them to make strategic investments for the future success of the firm (Florek-Paszkowska et al., 2021). Any financial decision aimed at enhancing efficiency has a direct impact on the overall financial performance and value of the firm (Akbar et al., 2021). The firm performance is measured by Tobin's Q, the findings reveal a positive and statistically significant connection between financial flexibility and performance. The companies with

higher financial flexibility exhibit a substantially higher Tobin's Q compared to their less flexible counterparts (Kumar & Vergara-Alert, 2020).

Financially flexible firms have the option to use more debt if needed and demonstrate a more effective and adept approach to making investments when compared to firms that are heavily burdened by existing debt (Ferrando et al., 2017). Legesse and Guo (2020) stated that the high short-term solvency reduces the relationship between the Firm effectiveness and long-term financing, as high-productivity companies are likely to generate high cash flows and have more capacity for short-term financing. When making decisions about debt financing, managers should consider the firm's productivity level, among other things.

Financially flexible companies exhibit stable and superior financial performance as compared to other firms (Ali & Siddiqui, 2020). Financial stability becomes a prerequisite because finance experts anticipate that companies with financial flexibility are better prepared to navigate the unavoidable repercussions of economic shocks (Settembre-Blundo et al., 2021). Moreover, firms that adapt their dividend strategies based on the necessity to keep their financial flexibility (Ferrando et al., 2017; Kumar & Vergara-Alert, 2020).

Investment Activities and Financial Flexibility

The ability of a firm to make investments is closely linked to the worth of its financial flexibility. The investment effectiveness is related to deviations from the optimal level of investments (Cherkasova & Kuzmin, 2018). Setianto and Kusumaputra (2017) stated that firms with higher financial flexibility possess a distinct advantage in executing a greater number of investment opportunities compared to their less financially flexible firms. Islam et al. (2020) suggested that the connection between financial flexibility and investment effectiveness becomes particularly evident in the presence of market imperfections and during periods of crises.

Financially flexible firms reduced their dependency on internal financing sources due to the availability of unused debt capacities, facilitating easier access to external financing for investment projects (Botta, 2020). Firms with financial flexibility in developing nations are also able to enhance their investment capabilities because financial flexibility enables businesses to invest more regularly and grab opportunities as they arise (Kedzior et al., 2020).

Financially flexible firms experienced more accessibility to investment options within financial markets. Financial flexibility plays an integral role in the decisions related to a firm’s capital structure, and future investments.

The financial flexibility lies in its capacity to reduce the decline in a firm's investments when faced with restricted financial support, thereby minimizing the reliance on external financing (Choi et al., 2021). Zhang et al. (2020) argued that the low profitability can be attributed in a significant way to a lack of financial flexibility, even in cases where companies can obtain capital through attractive tax savings options. Nugroho (2020) suggested that maintaining an adequate cash reserve enables companies to make investments in profitable projects without depending on costly external financing or reducing dividend payouts (Barry et al., 2022).

Firms possessing financial flexibility can get through challenging periods and grasp unexpected investment opportunities effortlessly, as they encounter no hurdles in securing funds to recover from losses (Putri & Willim, 2023). Arefieva et al. (2018) argued that a company's investment and strategic development plans will also affect its financial stability because it is difficult for firms to raise substantial amounts of capital in a short time when investment chances arise in the face of pricing volatility. Cherkasova and Kuzmin (2018) stated that financial flexibility is particularly beneficial for making good decisions about

debt, equity, and investments as well as for the overall success of the company (K. I. Khan et al., 2021). Xie and Zhao (2020) argued that financial flexibility supports the business in a situation of greatest uncertainty and helps to reduce the risk to the company's reputation. Al-Slehat (2019) investigated that the financial flexibility theory significantly increased investment spending; nevertheless, they are not concerned about the availability of internal financing because their investment is mostly based on the investment opportunities that the recession presents. Companies with financial flexibility are more efficient in capitalizing on investment opportunities, leading to enhanced profitability. Therefore, financial flexibility and investment opportunities are positively related to each other (Aslani & Zanjirdar, 2014).

Firm Performance and Financial Flexibility

The performance of a firm is a measure of achieving financial goals. Firm performance is closely referred to the concept of financial flexibility, which denotes a company's capacity to adjust and respond to changing circumstances in the financial landscape. Therefore, financially flexible firms should perform better and more steadily than other firms (Ma & Jin, 2016). Zhang et al. (2020) stated that the long-term performance of financially flexible firms is better than the market's (Ali & Siddiqui, 2020). Singla and Mallik (2021) suggested that business owners need to consider profitability as a key financial management goal to maximize their wealth. Financially flexible firms perform well, and this can be attributed to the positive relationship between financial flexibility and overall firm performance. The more a company embraces financial flexibility, the higher its level of performance tends to be (Mahmood et al., 2018).

A firm's performance and its financial strategy are positively correlated, determined by the scale and effectiveness of the investment strategy (Šmejkal et al., 2022). Firms that place a higher priority on financial flexibility typically perform better than those with less flexibility. The effectiveness of a company's performance is significantly influenced by its adeptness in hunting financing opportunities, as it is a crucial component in the association of economic flexibility and a company can enhance its performance efficiently by maintaining a high level of flexibility (Bolton et al., 2011; Edgeman, 2018; Mahmood et al., 2018). Zainudin et al. (2017) investigated the relationship between debt financing and a firm's economic performance with the use of financial flexibility. This indicates that Financial resilience plays an important part in converting the negative association between debt financing and economic performance into a positive one.

The firm performance and effectiveness of the investments are significantly enhanced by financial flexibility (Ma & Jin, 2016; Yi, 2020). Yanti et al. (2022) conducted the study based on free cash flows and established the findings that managers might take advantage of the concept of financial flexibility by making strategic use of internal funding the objective is to optimize the resources within their authority, thus enhancing overall firm performance. Financial flexibility emerges as a critical enabler, empowering firms to strategically invest in their future (Zolfigol & Zolfigol, 2019). Furthermore, companies with greater financial flexibility enjoy easy access to foreign capital markets, providing them with the necessary resources to not only navigate unforeseen challenges but also capitalize on unexpected opportunities and direct them toward value-adding projects and profitable businesses (Al-Slehat, 2019).

Firms that are financially flexible perform better than those that are not flexible. Therefore, there is a direct correlation between financial flexibility and firm performance because financial flexibility has a positive impact on performance (Raza et al., 2021). Financial flexibility is an important factor in assessing and influencing the firm performance and investment decisions. Therefore, based on the literature review the following hypotheses are:

H 1: Financial flexibility positively impacts on Investment activities of the automobile sector of Pakistan.

H2: Financial flexibility positively impacts on the Firm performance of the automobile sector of Pakistan.

Material and Methods

Data Collection

The secondary data for the variables were collected from the published annual reports of the automobile companies over the period 2013 to 2022. The sample size of this study consisted of 19 automobile-listed companies, and the total observations are equal to 190. The dependent variable of this study is financial performance which is further classified into two parameters Investment Activities and Firm Performance. Moreover, Firm performance is further measured by Tobin's Q which examines the performance of the firm based on the market value and Return on Assets (ROA). The Independent variable is financial flexibility which is measured by three parameters cash flows, debt levels, and access to market capitalization we also considered other control variables such as firm size, liquidity, and tangibility.

Table 1
Variables Calculation

Variables	Measurement Method	Symbol	Reference
Dependent Variables			
Financial Performance			
Investment Activities	Capital expenditure divided by Total assets	IA	(Setianto & Kusumaputra, 2017), (Danso et al., 2019), (Sulong et al., 2018), (Jabbouri & Almustafa, 2021), (Chang & Ma, 2019)
Firm Performance Tobin Q	The market value of equity and book value of its assets.	MB	(Altaf, 2020), (Setianto & Kusumaputra, 2017), (Sulong et al., 2018), (Kaushik & Chauhan, 2019), (Daud et al., 2016), (Al-Slehat, 2019), (Mahmood et al., 2018), (Mahmood et al., 2022), (Ahmed et al., 2022), (Ball et al., 2020)
Return on assets	Net profit earned by a company divided by Total assets	ROA	
Independent Variable			
Financial flexibility			
Cash flows	Net cash flows (Operating, Investing, and Financing Activities)	NCF	(Al-Slehat, 2019), (Hegde et al., 2023), (Jabbouri & Almustafa, 2021), (Legesse & Guo, 2020), (H. u. R. Khan et al., 2021), (Kumar & Vergara-Alert, 2020), (Mahmood et al., 2021), (Chang & Ma, 2019), (Altaf, 2020), (Feng et al., 2022), (Nnadi et al., 2022),
Debt Levels	Debt to equity ratio = Non-current liabilities divided by Total shareholders' equity	DL	(Judge & Korzhenitskaya, 2022), (Raza et al., 2021), (Setianto & Kusumaputra, 2017), (Yeniaras et al., 2021), (Lambrinoudakis et al., 2019), (Al-Slehat, 2019), (Mahmood et al., 2018), (Fahlenbrach et al., 2021), (Islam et al., 2019), (Kumar & Vergara-Alert, 2020), (Islam et al., 2022), (Yung et al., 2015), (Oad Rajput et al., 2019)
Access to capital market	Market capitalization = No of shares issued multiplied by Current market share price	MCAP	
Control Variables			
Firm Size	Log of Total Assets	FS	

Liquidity	Current ratio = Current assets divided by Current Liabilities	Liq	(Hegde et al., 2023), (Mahmood et al., 2018), (Chang & Ma, 2019), (Batool et al., 2022)
Tangibility	Total Fixed assets divided by Total assets	Tang	

Model Specification

This study is centered on constructing a model to empirically assess the influence of financial flexibility on financial performance. Financial performance, being a crucial factor, significantly contributes to enhancing the overall value of a company. The following dynamic panel model was created for empirical testing.

$$FP_{it} = \beta_1 FP_{it-1} + \beta_2 FF_{it} + \beta_3 NCF_{it} + \beta_4 DL_{it} + \beta_5 MCAP_{it} + \beta_6 FS_{it} + \beta_7 Liq_{it} + \beta_8 Tang_{it} + \varepsilon_{it} \quad (1)$$

In this regression model, the study includes the lag value of dependent variables as an independent variable by using a dynamic panel model. The purpose of using this model is to study how firms' performance is affected by mean reversion behavior. This analytical method indicates that a company's success in past years affects its performance from the current year by offering the adjustment speed of performance. FP_{it} denotes financial performance, FF_{it} represents financial flexibility, NCF_{it} represents net cash flows, DL_{it} denotes debt levels, $MCAP_{it}$ denotes market capitalization, FS_{it} denotes firm size, Liq_{it} denotes liquidity, and $Tang_{it}$ denotes tangibility.

$$IA_{it} = \beta_1 IA_{it-1} + \beta_2 FF_{it} + \beta_3 NCF_{it} + \beta_4 DL_{it} + \beta_5 MCAP_{it} + \beta_6 FS_{it} + \beta_7 Liq_{it} + \beta_8 Tang_{it} + \varepsilon_{it} \quad (2)$$

IA_{it} represents investment activities, FF_{it} represents financial flexibility, NCF_{it} represents net cash flows, DL_{it} denotes debt levels, $MCAP_{it}$ denotes market capitalization, FS_{it} denotes firm size, Liq_{it} denotes liquidity, and $Tang_{it}$ denotes tangibility.

$$MB_{it} = \beta_1 MB_{it-1} + \beta_2 FF_{it} + \beta_3 NCF_{it} + \beta_4 DL_{it} + \beta_5 MCAP_{it} + \beta_6 FS_{it} + \beta_7 Liq_{it} + \beta_8 Tang_{it} + \varepsilon_{it} \quad (3)$$

Firm performance denotes Tobin Q which is measured by Market to book value $MB_{it,}$ FF_{it} represents financial flexibility, NCF_{it} represents net cash flows, DL_{it} denotes debt levels, $MCAP_{it}$ denotes market capitalization, FS_{it} denotes firm size, Liq_{it} denotes liquidity, and $Tang_{it}$ denotes tangibility.

Statistical Analysis

In conducting empirical hypothesis estimations, this study used a dynamic panel model, incorporating lag values of the dependent variable as independent variables (Labra & Torrecillas, 2018). Despite the absence of serial correlation in the error term, the dynamic panel model introduces a notable correlation between the error term and lagged dependent variables. In the context of dynamic panel data, violations of assumptions related to serial correlation in the error term can occur. Fixed and random effects methodologies prove inadequate for addressing this issue within the dynamic regression model due to the correlation between lagged regressors and error terms. To tackle these methodological challenges associated with dynamic panel data, the study chose to utilize the Generalized Method of Moments (GMM).

Diagnostic Test

In establishing the validity of the model, this study employed a set of tests to ensure the reliability of instrumental variables and to verify the normal distribution of the model (Larcker & Rusticus, 2010). Initially, the study conducted tests for the absence of serial correlation among the error terms, utilizing both first and second-order serial correlation tests.

Additionally, the exogeneity of instruments was thoroughly tested through Sargan and Hansen tests, ensuring the absence of over-identified restrictions and validating that instruments were non-correlated with the error term. This comprehensive set of tests enhances the overall resilience and reliability of the model, affirming its validity in capturing the relationships between variables under examination.

Results and Discussion

Descriptive Statistics

Descriptive statistics is a set of analytical techniques which is used to summarize and describethe essential features of a dataset. Descriptive statistics is used to identify the trends and outliers. The data sample of this study summaries the observation, mean, standard deviation, minimum and maximum values of the variables. The results are presented in Table 2.

The result showed that net cash flows has an average value of 0.350 with a standard deviation of 0.350 which indicated an average positive cash flow with considerable variability between the observations. The average value of debt levels is 0.485 with a standard deviation of 0.137 which indicates that there is an average portion of equity 48.5% used for his debts. The average value of market capitalization is 0.877 while it has a standard deviation of 0.692. The result showed that the average value of Investment activities in the automobile sector is 0.277 with a standard deviation of 0.725. The average value of Tobin Q is 0.343 with a standard deviation of 0.993 which indicates the considerable variation in firms' market valuation relative to their assets. On the other hand, the average value of Return on assets is 0.182 while the standard deviation is 0.330. Automobile firms maintain net earnings of 18.2% of their total assets.

Table 2
Descriptive Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
NCF	190	0.350	0.350	0.011	1.802
DL	190	0.485	0.137	0.172	0.635
MCAP	190	0.877	0.692	0.050	2.890
IA	190	0.277	0.725	-1.685	4.518
TQ	190	0.343	0.993	0.000	4.427
ROA	190	0.182	0.330	-0.306	2.945
FS	190	7.220	0.942	5.373	9.960
LIQ	190	1.612	1.68	0.102	8.761
Tang	190	0.356	0.186	0.246	0.987

Note: Table 2 reports the descriptive analysis of variables used in the model for automobile firms during 2013-2022.

Correlation Analysis

Correlation analysis is a statistical technique used to determine the relationship between variables. It demonstrates how one affects the other variable if there is a correlation between the two variables. The correlation may be a perfect positive or negative correlation, partial correlation, and no correlation. The correlation analysis in this study is among the explanatory variables and dependent variables.

Table 3 shows that Debt levels have a negative correlation with Net cash flows (-0.018) further MCAP has a positive correlation with Net cash flows (0.095). There is a positive correlation between Investment activities and Net cash flows (0.046), and Tobin Q has a positive correlation with NCF (0.019). Return on assets has a positive correlation with NCF (0.016), Firm size has a positive correlation with Net cash flow (0.045), Liquidity has a positive correlation with NCF (0.032) and there is a positive correlation between Tangibility and Net cash flows (0.020).

Market Capitalization has a negative correlation with debt levels (-0.045), Investment activities have a negative correlation with DL (-0.014), Tobin Q has a negative correlation with debt levels (-0.027). There is a positive correlation between Return on assets and Debt levels (0.0497) (Iqbal & Usman, 2018; Lestari, 2021). It indicates that as the level of debt increases, the return on assets also tends to increase. This relationship indicates that companies with higher levels of debt are likely to generate higher returns on their assets. Furthermore, debt can be effectively utilized to finance operations and investments that lead to increased profitability. Rehman (2013) stated that there is a positive relationship between financial leverage and financial performance.

Table 3
Correlation Analysis

	NCF	DL	MCAP	IA	TQ	ROA	FS	Liq	TANG
NCF	1								
DL	-0.018	1							
MCAP	0.095	-0.045	1						
IA	0.046	-0.014	0.017	1					
TQ	0.019	-0.027	0.012	0.020	1				
ROA	0.016	0.0497	0.023	0.019	0.027	1			
FS	0.045	-0.029	0.012	0.028	0.025	0.076	1		
Liq	0.032	-0.020	0.044	-0.026	0.026	0.007	0.015	1	
TANG	0.020	-0.011	0.027	0.024	0.038	0.043	0.021	0.013	1

Note: "***'", "**", and "*" showed the significance level at 1%, 5%, and 10% respectively. Table 5 presents the correlation analysis between the dependent variable and explanatory variables. It presents the direction of the relationship between the variables that are used in the current study. The correlation is among Net Cash Flows, Debt Levels, Market Capitalization, Investment Activities, Tobin Q, Return on Assets, Firm size, Liquidity, and Tangibility.

Investment Activities and Financial Flexibility

Table 4 shows that the lag value of the dependent variable is incorporated as an independent variable to create a dynamic panel model. The results indicate that the lagged value of the dependent variable has a significant impact on current value of Investment activities. This demonstrates that the model is in dynamic nature. Moreover, the current investment decisions are affected by the previous investment decisions of firms and the mean reversion behavior of investment decisions.

This table shows that the lagged value of Investment activities which has a positively significant impact on the current value. This indicates that the past levels of Investment Activities have a significant positive effect on current Investment Activities. The coefficient of Net cash flows has a significant positive impact on investment activities of automobile firms. This indicates that higher net cash flow levels are linked to more investment activity which means that companies with higher cash flows usually make more investments in their operations or growth opportunities (Sitompul & Khadijah, 2020).

Moreover, Market capitalization indicates that there is a positively significant impact between market capitalization and investment activities. The findings of this study shows that larger market capitalization is associated with higher levels of investment activities (Farooq et al., 2022). The degree of financial leverage has a significant negative impact on investment activities. This indicates that higher leverage tends to have a negative impact on investment activities.

Table 4
Estimation results of equation 1 of Investment activities based on financial flexibility

Variables	IA	IA
Constant	-0.035	0.010
	(0.053)	(0.147)

$IA_{(t-1)}$	0.484***	0.276***
	(0.049)	(0.024)
NCF	0.161***	0.246***
	(0.055)	(0.041)
MCAP	0.087**	0.051***
	(0.032)	(0.017)
Degree of Financial Leverage	-0.030***	-0.004**
	(0.011)	(0.038)
Liquidity		-0.019***
		(0.007)
Firm Size		0.069***
		(0.007)
Tangibility		-0.142
		(0.100)
Table: 'c' Time Dummy	Yes	Yes
AR(1)	0.00	0.00
AR(2)	0.211	0.689
Sargan / Hansen Test Over identify	0.689	0.294
Number of Obs	190	190
Number of firms	19	19

Note: Table 4 presents the results related to the two-step system GMM dynamic panel model. Independent variable is financial flexibility which represents year-wise standard deviation from 2013 to 2022. The significant value of AR (1) shows the presence of first order serial correlation that null hypothesis of no first difference autocorrelation among the error component is rejected. AR (2) is insignificant which indicates that there is no second order serial correlation between the error terms in the regression level and Sargan / Hansen test overidentifying value indicates that the instruments are valid and do not exhibit over identification. The results of AR (1), AR (2) and Sargan / Hansen test shows overall that GMM is correctly described and has no identification problems. The table represents the significance level "***", "**", and "*" at 1%, 5%, and 10% respectively.

ROA and Financial Flexibility

The results related to the impact of Financial flexibility measured by the standard deviation of Return on assets are presented in Table 5. In this analysis, the lag value of the dependent variable is incorporated as an independent variable to create a model as a dynamic panel model. Table 7 presents the lagged value of return on assets which has a positively significant impact on the current value. This finding shows that the past levels of firm performance have a significant positive effect on current firm performance. This table shows that the Net cash flows has a positively significant impact on return on assets.

Market capitalization tends to have a significant positive impact on return on assets. A higher market capitalization indicates that companies are performing well and that the market is pricing their stocks appropriately. It usually leads to more financial flexibility which is more likely to increase the firm's performance (Omidiji et al., 2020).

Moreover, the degree of financial leverage has a positive significant impact on return on assets. This indicates that an increase in the degree of financial leverage allows a firm to increase its return on assets by utilizing debts to finance investments that generate higher returns than the cost of debt (Lestari, 2021).

Table 5
Estimation results of equation 2 of Return on assets based on financial flexibility

Variables	**ROA**	**ROA**
Constant	0.027***	-0.333***
	(0.008)	(0.068)
$FP_{(t-1)}$	0.530***	0.0515***
	(0.037)	(0.020)

NCF	0.081***	0.0732***
	(0.015)	(0.010)
MCAP	0.060***	0.029***
	(0.013)	(0.008)
Degree of Financial Leverage	0.025***	0.151***
	(0.007)	(0.044)
Liquidity		0.003***
		(0.001)
Firm Size		0.038***
		(0.006)
Tangibility		0.015
		(0.035)
Time Dummy	Yes	Yes
AR(1)	0.00	0.00
AR(2)	0.094	0.091
Sargan / Hansen Test Over identify	0.168	0.366
Number of Obs	190	190
Number of firms	19	19

Note: "***'", "**", and "*" showed the significance level at 1%, 5%, and 10% respectively.

Tobin Q and Financial Flexibility

Table 6 presents the lagged value of return on assets which tends to have a positively significant impact on the current value of Tobin Q. Moreover, the coefficient of Net cash flows tends to have a positive significant impact on Tobin Q which indicates that there is a strong relation between the company's cash flow and market value which reflects the greater investors' confidence (Al-Nasser Abdallah et al., 2020). The market capitalization has a positive significant impact on firm performance (Tobin Q). This suggests that a higher growth rate in market capitalization often corresponds to increased profitability for a firm, resulting in enhanced firm performance and shareholder value.

Furthermore, the coefficient Degree of financial leverage tends to have a negative impact on Tobin Q which indicates that higher levels of debt are associated with lower market valuation. Debt levels have a negative effect on Tobin Q, suggesting that investors consider businesses with higher debt levels to be riskier or less valuable investments (Cardao-Pito, 2022).

Table 6

Estimation results of equation 3 of Tobin Q based on financial flexibility

Variables	**TQ**	**TQ**
Constant	0.191	-0.140
	(0.105)	(0.105)
$FP_{(t-1)}$	0.781***	0.852***
	(0.042)	(0.014)
NCF	0.131***	0.351***
	(0.045)	(0.031)
MCAP	0.079***	0.065***
	(0.031)	(0.016)
Degree of Financial Leverage	-0.034***	-0.057
	(0.007)	(0.057)
Liq		0.007**
		(0.003)
Firm Size		0.012***
		(0.008)
Tangibility		0.529***
		0.060
Time Dummy	Yes	Yes
AR(1)	0.00	0.00
AR(2)	0.00	0.06

Sargan / Hansen Test Over identify	0.082	0.239
Number of Obs	190	190
Number of firms	19	19

Note: "***'", "**", and "*" showed the significance level at 1%, 5%, and 10% respectively

Table 7
Summary of relationship tested through Hypotheses

Hypothesis	Description	Expected sign	Empirical Findings	Supported
H1	Net cash flows has a significant positive impact on Investment activities (IA) of automobile firms listed on Pakistan Stock Exchange.	+	+	Yes
H2	Net cash flows has a significant positive impact on Return on assets (ROA) of automobile firms listed on Pakistan Stock Exchange.	+	+	Yes
H3	Net cash flows has a significant positive impact on Tobin "Q" of automobile firms listed on Pakistan Stock Exchange.	+	+	Yes
H4	Debt levels has a significant negative impact on Investment activities (IA) of automobile firms listed on Pakistan Stock Exchange.	-	-	Yes
H5	Debt levels has a significant positive impact on Return on assets (ROA) of automobile firms listed on Pakistan Stock Exchange.	-	+	No
H6	Debt levels has a significant negative impact on Tobin "Q" of automobile firms listed on Pakistan Stock Exchange.	-	-	Yes
H7	Market capitalization has a significant positive impact on Investment activities (IA) of automobile firms listed on Pakistan Stock Exchange.	+	+	Yes
H8	Market capitalization has a significant positive impact on Return on assets (ROA) of automobile firms listed on Pakistan Stock Exchange.	+	+	Yes
H9	Market capitalization has a significant positive impact on Tobin "Q" of automobile firms listed on Pakistan Stock Exchange.	+	+	Yes

Conclusion

The study analyzes the nexus between financial flexibility and financial performance of automobile firms from an Asian perspective over the period 2013 - 2022 in a dynamic panel model. The analysis of the literature shows a strong correlation between financial performance and financial flexibility.

The findings suggest that Financial flexibility tends to have a positive impact on Financial performance which indicates that firms with greater financial flexibility tend to demonstrate higher levels of performance by providing theoretical support for the trade-off theory, and theory of investment. The first objective of this study is to analyze the impact of net cash flows on financial performance. Net cash flows significantly increase the financial performance. Secondly, to addresses the impact of Debt levels on the financial performance of automobile firms. This study analyzes that the degree of financial leverage tends to have a negative impact on investment activities and firm performance (Tobin Q) but there is a positive impact of the degree of financial leverage on return on assets. In this regard, this study rejects the null hypothesis and accepts the alternative hypothesis that the degree of financial leverage positively impacts on return on assets.

Firms with higher levels of debt are more likely to generate higher profits by utilizing debts in financing operations which leads to an increase the profitability and firm performance. Furthermore, this study analyze that market capitalization tends to have a significantly positive impact on financial performance which indicates that firms respond to high market capitalizations by increasing their profitability. Moreover, this study helps corporate managers to get useful information which is directly impacts on their decision-making processes, reduces their risk of financial distress, and improves the firm's performance. This study also encourages future researchers to examine the impact of financial flexibility on financial performance in different manufacturing sectors and may explore the comparative analysis between financial and non-financial firms in the context of financial flexibility.

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