



The primary focus of this thesis is to investigate whether Indonesian firms are inert towards the readjustment of capital structure. The Fama-Macbeth regression is utilized as a means to estimate the relevance of stock return towards the current leverage ratio. The findings suggest a near 1-to-1 co-movement between stock return and capital structure over a one-year horizon. While in the longer horizon the co-movement diminished, and past debt ratio, as well as a static target ratio, has become increasingly important. Thus, this suggests a non-readjustment behavior. Moreover, this behavior also persists in firms who experienced stock price changes continuity (current and future price changes in the same direction). Interestingly, Indonesian firms are actively issuing debt and equity, which can cut more than half of the stock return induced capital structure changes in the 5-year horizon. Thus, these findings suggest that Indonesian firms are not inert but instead have a slow readjustment behavior. However, corporate issuing motives remain to be a mystery.

**Keywords:** Capital structure, stock return, readjustment, inertia