We examine how production flexibility affects financial leverage. A worldwide sample of energy utilities allows us to apply direct measures for production flexibility based on their power plants. We find that production flexibility increases financial leverage. For identification, we exploit privatizations and deregulations of electricity markets, geographical variations in natural resources, the technological evolution of gas-fired power plants, and differences in electricity prices and recapitalization cost across regions. Production flexibility affects financial leverage via the channels of reduced expected cost of financial distress and higher present value of tax shields. The relative importance of these channels depends on firms’ profitability.