A STUDY ON CAPITAL STRUCTURE ANALYSIS AND SM EXPORTS PROJECT REPORT FOR SM EXPORTS

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ABSTRACT

This paper analyzes the explanatory power of some of the recent theories of optimal capital structure. The study extends empirical work on capital structure theory in three ways. First, it examines a much broader set of capital structure theories, many of which have not previously been analyzed empirically. Second, since the theories have different empirical implications in regard to different types of debt instruments, the authors analyze measures of short-term, long-term, and convertible debt rather than an aggregate measure of total debt. Third, the study uses a factor analytic technique that mitigates the measurement problems encountered when working with proxy variables.

IN RECENT YEARS, A number of theories have been proposed to explain the variation in debt ratios across firms. The theories suggest that firms select capital structures depending on attributes that determine the various costs and benefits associated with debt and equity financing. Empirical work in this area has lagged behind the theoretical research, perhaps because the relevant firm attributes are expressed in terms of fairly abstract concepts that are not directly observable.

1. INTRODUCTION

OVERVIEW OF CAPITAL STRUCTURE ANALYSIS

Capital structure can be defined as the mix of owned capital (equity reserves &surplus) and borrowed capital debentures, loan from bank, financial institutions .maximization of share holder's wealth is prime objective of a financial manager .the same may be achieved if an optimal capital structure is designed for the company. Planning a capital structure is a highly psychological, complex &qualitative process .it involves balancing the shareholder's expectation (risk& return)&capital requirement of the firm. The capital structure is how a firm finances its overall operation &growth by using different sources of funds. Debt comes in the form of bond issues or long term notes payable while equity is classified as common stock, preferred stock or retained earnings. Compute the financial leverage index, debt to capital ratio, debt to equity ratio &other techniques for analyzing capital structure. Clarifying capital structure related terminology the equity part of the debt-equity relationship is the easiest to define in a company's capital structure equity consists of a common &preferred stock plus retained earnings, which are summed up in the shareholders equity account on a balance sheet.

The term capital structure refers to the percentage of capital (money) at work in a business by type. Broadly speaking, there are two forms of capital: equity capital and debt capital. Each type of capital has its own benefits and drawbacks and a substantial part of wise corporate stewardship and management is attempting to find the perfect capital structure in terms of risk/reward payoff for shareholders. This is true for Fortune 500 companies and for small business owners trying to determine how much of their start-up money should come from a bank loan without endangering the business.

Equity Capital

Equity capital refers to money put up and owned by the shareholders (owners). Typically, equity capital consists of two types: 1. contributed capital, which is the money that was originally invested in the business in exchange for shares of stock or ownership and 2. retained earnings, which represents profits from past years that have been kept by the company and used to strengthen the balance sheet or fund

growth, acquisitions, or expansion. Many consider equity capital to be the most expensive type of capital a company can utilize because its "cost" is the return the firm must earn to attract investment. A speculative mining company that is looking for silver in a remote region of Africa may require a much higher return on equity to get investors to purchase the stock than a firm such as Procter & Gamble, which sells everything from toothpaste and shampoo to detergent and beauty products.

Debt Capital

The debt capital in a company's capital structure refers to borrowed money that is at work in the business. The safest type is generally considered long-term bonds because the company has years, if not decades, to come up with the principal while paying interest only in the meantime. Other types of debt capital can include short-term commercial paper utilized by giants such as Wal-Mart and General Electric that amount to billions of dollars in 24-hour loans from the capital markets to meet day-to-day working capital requirements such as payroll and utility bills. The cost of debt capital in the capital structure depends on the health of the company's balance sheet — a triple AAA ratedfirm is going to be able to borrow at extremely low rates versus a speculative company with tons of debt, which may have to pay 15 percent or more in exchange for debt capital.

2. LITERATURE REVIEW

Taub (1975) tried to ascertain the factors influencing a firm's choice of a debt equity ratio. For this study a total of 89 firms from Unites States were chosen randomly over a period of ten year from 1960 to 1969 and the likelihood-ratio statistics and t-test were used to test the hypothesis described therein. The empirical results of the study in terms of the expected sign of the co-efficient were mixed. The return to the firm, long term rate of interest, Bhat (1980) made an attempt to analyze the determinants of financial leverage and to investigate the relationship between the leverage ratio and institutional characteristics viz. firm size, variation in income, growth, profitability, debt service and dividend payout through correlation and regression analysis. The cross-section data for this study were collected for six years from 1973 to 1978 from only one industry i.e., Engineering Industry, so as to alleviate the effect of industry type on the financial leverage ratio. The study reveals that firm size, growth rate and the degree of operating leverage does not have any significant relationship with financial leverage whereas earnings rate, business risk, dividend payout ratio and debt service ratio have been found to be negatively related. Only the relation of operating leverage with leverage has been found positive but insignificant relationship. The study observed that the institutional characteristics are important determinants of financial leverage ratio.

Venkatesan (1983) tried to explore the relationship of certain exogenous variables with the financial leverage. He used the data of 66 firms from four different industries for a time span of four year from 1977 to 1980. He attempted to analyze the impact of seven different variables on financial structure of firms by using the multiple regression model, correlation and t-test. The study reveals that null hypothesis proposed in the study that size does not have any relationship with financial leverage could not be rejected for any of the industries. Coverage ratios revealed the significant relationship to the financial structure in all the industries except for steel industry in intra-industry model during study period. Business risk and growth was not found significantly related to financial structure in any of the industries examined. In the inter-industry model, low-levered firms revealed significant relationship between selected variables except growth ratio and financial leverage. But medium and high levered firms were not having any significant common determinant of their financial structure.

Titman and Wessels (1988) introduced a factor analysis technique for estimating the impact of unobservable attributes on the choice of corporate debt ratio using the data from the 469 UK firms for the period of nine years from 1974-82. The study found that debt levels are negatively related to uniqueness of a firm's line of business. The results also indicate that transaction costs may be an important determinant of capital structure choice and short term debt ratios were shown to be negatively related to firm size. Non-debt tax shield, volatility, collateral value and future growth have not any significant impact on debt ratios.

3. INDUSTRY PROFILE

Description The history of the SM EXPORTS and garment industry lies in an almost 10 year's period of state owned enterprises, which operated under the centralized socialist economy. The previous industry production was derived through a large domestic valued added chain that used to produce from fiber until final product. Industry mainly supplied the domestic market, while exports were managed by a single government agency.

After2010, most of the enterprises went through a privatization process. A significant part of these enterprises didn't change their destination, they kept producing textiles and garments but their activity was now concentrated on production under outward processing regime of clothes which comprise the majority of the SM EXPORTS. The industry inputs are mainly supplied by imports, using the cheap labour advantage. The garment firms have no special technological processes, no marketing strategies and poor vertical integration, consequently leaving abroad most of the value added in this sector.

This industry plays an important role in the country economy as shown in table1.

Table 1: key indicators for textile/garment industry

General data	2012	Manufact industry	2013	Manufact industry	2014	Manufact industry	2015	Manufact industry
Production (in mln leke)	3,235	8%	4,245	10%	4,935	9%	6,673	11%
No.of Employees	8,626	24%	9,129	25%	8,865	27%	1,212	30%
No.of Firms	327	9%	347	10%	298	8%	407	11%
Investment Rate(in mln Leke)	690	19%	616	7.6%	477	4%	558	7%

Source: INSTAT,2012-2015

4. EXECUTION

4.1.DATA COLLECTION METHOD

There are primary and secondary source of data source

PRIMARY SOURCE

Primary data is information that you collect specifically for the purpose of your research project .an advantages of primary data is that it is specifically tailored to your research needs. A disadvantage is that it is expensive to obtain.

SECONDARY SOURCE

Company's internal records, publications, journals, web side are the main secondary source used. Reports showing the latest developments and changes in the overall organization were also used for the study.

Secondary data refers to data that was collected by someone other than the user. Common source of secondary data for social science include censuses, information collected by government departments, organizational records and data that was originally collected for other research purposes.

4.2.STATISTICAL TOOLS

- Current asset
- Liquid ratio
- Cash to working capital
- Gross profit ratio
- Net profit ratio
- Trend analysis
- Cash in hand
- Trend on working capital

Co-efficient of correlation

- Correlation b/w cash and net profit
- Correlation b/w cash and sales

Least square method

Least square method of net profit trend method

4.3.RESEARCH TOOLS

This part of study is mainly focused on verifying main objectives of study. Researcher used **ratio analysis , correlation** and **graphs** as statistical tool for analysis of data

HYPOTHSIS

Ho: There is no association between cash position and net profit.

H1: There is no association between cash position and net profit.

There is no relationship between cash position and net profit.

There is no relationship between cash position and sales

5. DATA ANALYSIS

CURRENT RATIO

Current ratio is the most common ratio for measuring liquidity. It represents the "**ratio of current assets to current liabilities**". It is also called working capital ratio. It is calculating by dividing current assets by current liabilities

$$\text{Current ratio} = \frac{\text{Current asset}}{\text{Current liabilities}}$$

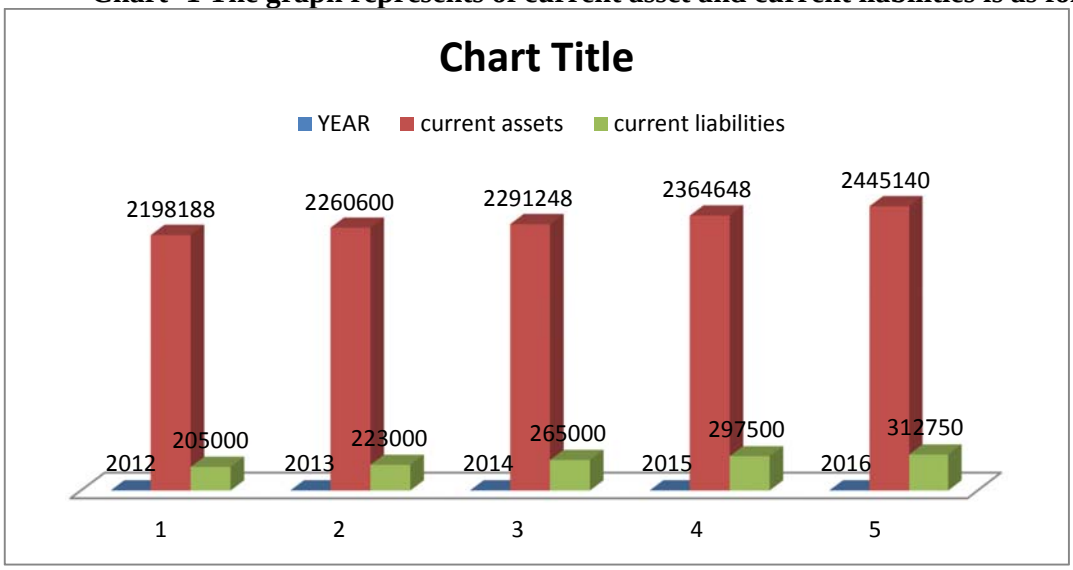
Current assets are those, the amount of which can be realized with in a period of one year in includes cash in hand, cash at hand etc. Current liabilities are those amounts which are payable with in a period of one year-current liabilities are creditors, bills payable etc. The current ratio of the firm measures its short term solvency, ie, its ability to meet short term obligations. In a sound business a current ratio of 2:1 is considered an idle one. It provides a margin of safety to the creditors

Table 2 CURRENT RATIO

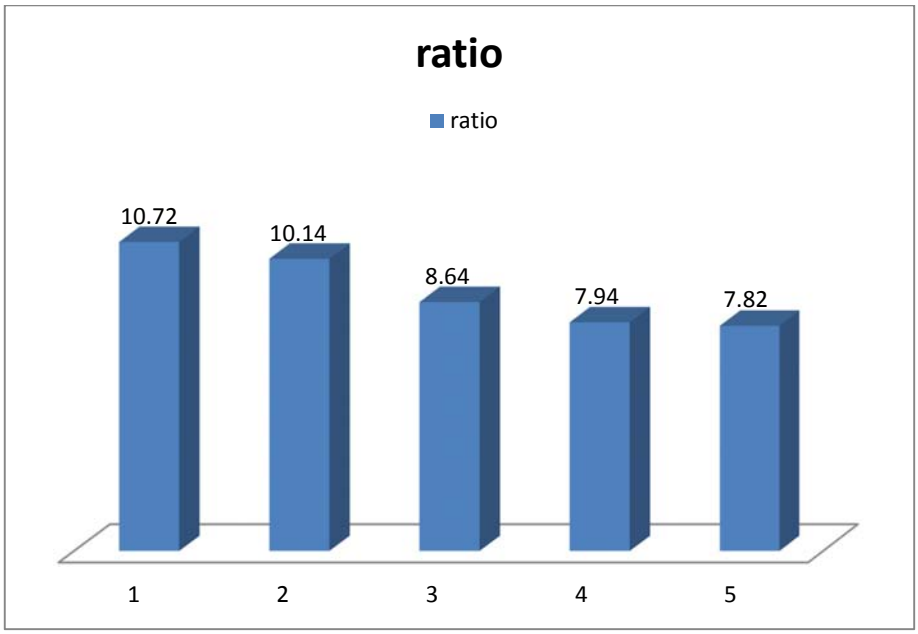
Year	Current assets	Current liabilities	ratio
2012	2198188	205000	10.72
2013	2260600	223000	10.14
2014	2291248	265000	8.64
2015	2364648	297500	7.94
2016	2445140	312750	7.82

SOURCE : COMPUTED TABLE

Chart -1 The graph represents of current asset and current liabilities is as follows.



The following chart shows the ratios of the past five years



INTERPRETATION

From the above table and form the above chart 1.2. it can be seen that the current ratio during the year 2012 was 10.72 and in 2013 it was an decreased to 10.14 while during the year 2014 there was a decreases in to 8.64 during the year 2015the current ratio was decreased to 7.94 but in the case of 2016 the final year it was a slight decrease to 7.82 i.e. current assets double the current liability 9is considered to be satisfactory. But it can be analyzed from the above that except for the year 2012 the organization did not attained a satisfactory.

ABSOLUTE LIQUID RATIO

The ratio is obtained by dividing cash (of course cash in hand and cash at bank) and marketable securities by current liabilities. It is also known as cash position ratio.

$$\text{Absolute liquid ratio} = \frac{\text{Cash + marketable securities}}{}$$

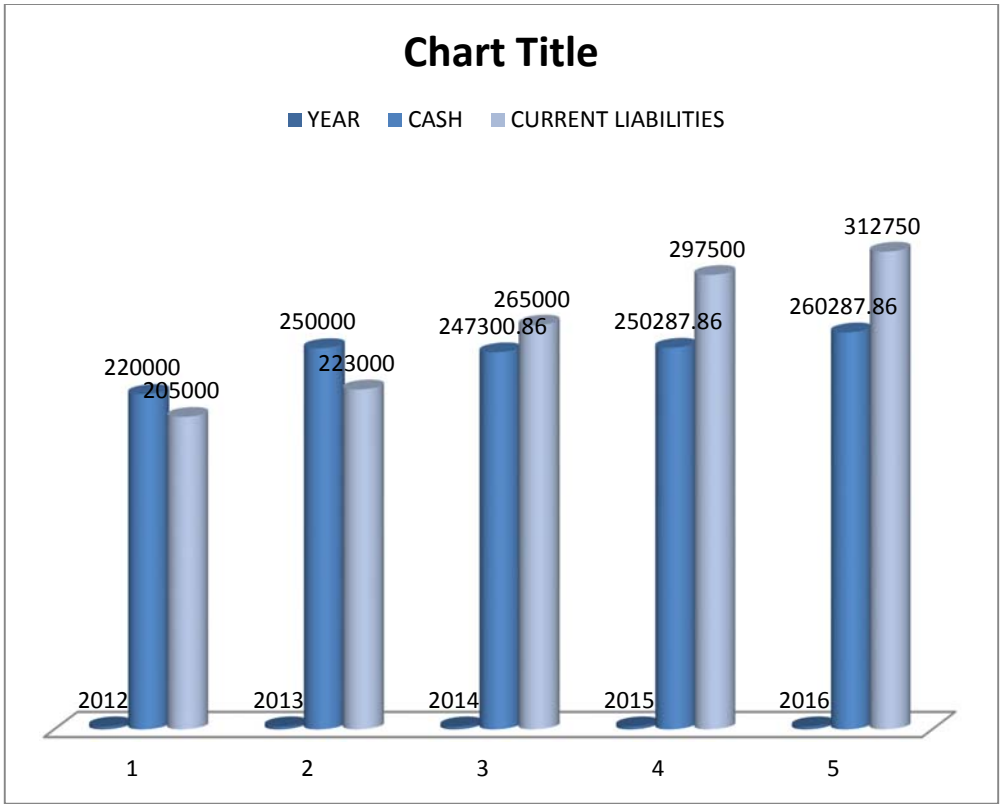
Table 2 LIQUID RATIO

Year	cash	Current liabilities	Ratio
2012	220000	205000	1.07
2013	250000	223000	1.12
2014	247300.86	265000	0.93
2015	250287.86	297500	0.84
2016	260287.86	312750	0.83

SOURCE: COMPUTED TABLE

The Current liabilities and Absolute Liquid Ratio can be expressed in this chart

Chart 2



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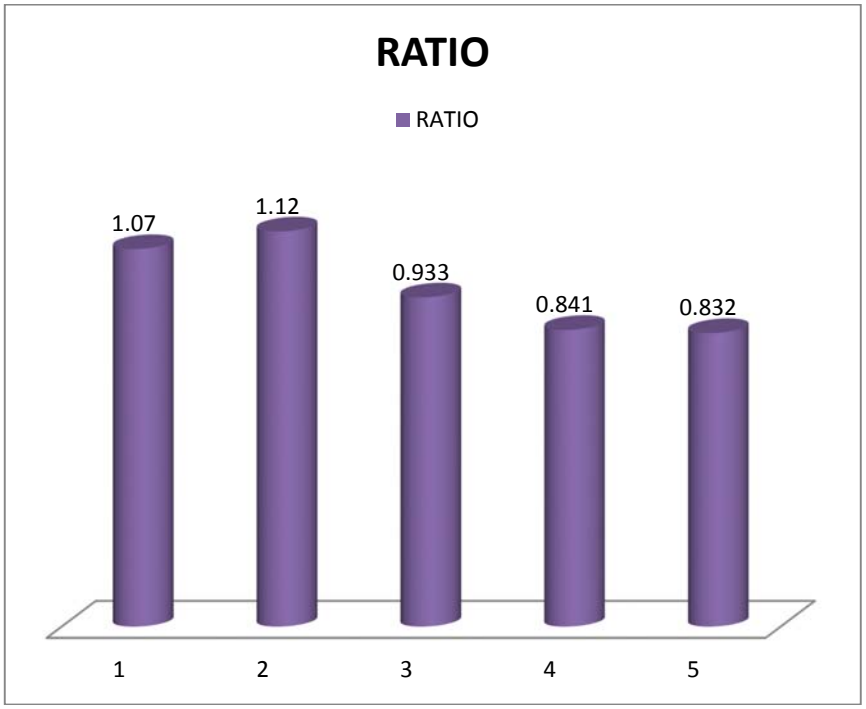

INTERPRETATION

We have to seen from the above table and from the above chart that the absolute liquid ratio during the year 2012 was 1.07 and the subsequent year 2013 the ratio has a increase to 1.12. While during the year 2014 the ratio has its maximum in last five years to 0.933 but in 2012 it has decreases to 0.841. In 2016 also it has slight decreases to .0.832.

6. CONCLUSION

Since the ability to access capital directly affects the value of a business, owner-managers need to understand the ramifications of this value-capitalization relationship in the private capital markets. The previous chapters described the fundamental concepts underlying the capitalization of private businesses. This chapter builds on these fundamentals with a discussion of these issues:

- Capital providers use credit boxes and other devices to manage risk and return in their portfolios.
- Expected returns to institutional capital providers comprise the Pepperdine Private Capital Market Line.
- Private cost of capital emanates from the private capital markets.

High cost of capital limits private company value creation our hypothesis suggests that effective appraisal process correlates with a higher level of satisfaction and employee engagement. Engaged employees are those who are willing to invest additional efforts towards enhancing market position of their company and contribute to better financial results. This is their direct contribution to the company. Engaged employees are not only motivated to work but they also know exactly what to do and how to do it more effectively because they know the strategy and company objectives and share them. All this could possibly mean that the more engaged to the company people are, the better financial results are likely to be achieved. This correlation has been confirmed by many surveys conducted by consulting companies.

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