"Effect of Capital Structure Analysis on Kesoram Cement's"

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Abstract:

This paper is entitled to "Effect of Capital Structure analysis on Kesoram Cement's" gives the perception to the administration of a company to estimate the effect of capital structure on financial fulfillment of the company. Capital structure is mixing of long term sources of funds like equity shares, preference shares, and debentures to meet the required capital of the company. The financing of a capital formation choice is a critical administrative choice. This analysis has been made on the basis of Indifference point analysis and multivariate regression analysis. The financial position of the company is measured based on the earnings per share and returns on equity of the company.

Key words: Capital Structure, EBIT-EPS analysis, Returns on equity and Earnings per share.

I Introduction

Capital formation is a mixture of capital increment within the organization. That mixture or combination control the capital cost. Commonly capital formation is the mixture of debt and equity. The extent of this debt and equity to the full capital is chosen by methods of the organization as per the monitory function and capacity to raise such capital. That selection concerning the capital formation may be more critical because it impacts the income in keeping with proportion or the shareholders wealth. Capital structure selection is an important choice to extract by using each enterprise, the positives and negatives of those choices performs an essential position in figuring out destiny of each business. That current idea of formation of the capital became mounted by Modigliani and miller, there's no common ideology of debt and equity performance, and there is no motive to anticipate one. Various philosophies are regarding capital formation assist us recognize approximately the mix of debt equity selected by that companies. Those philosophies are classified into organizations either they are expecting the life of the greatest debt-equity ratio for every company or they reveal that there is no well-described intention capital formation.

Objectives of the Study

1. To examine capital structure of KESORAM CEMENTS with the assist of EBIT-EPS analysis.
2. To analyze the effect of financing decision on EBIT and EPS of the firm.
3. To identify the impact of debt on returns on equity of the company.

Need of the Study

In any organization the management involves in reducing the overall cost of capital that gives benefits to the investors to maximization of their wealth and also influence in the growth of the organization. The leverage influence on the capital cost and estimate the worth of an organization, the ideal capital formation might be received at that mix of debt and equity that improves the aggregate worth of that firm. To estimate the worth of the organization relies on its forecast income flow and that amount is utilized to limit that movement.

Scope of the Study

The scope of the study is analyzing the impact of capital formation of a company in order to meet the requirement of finance of that company.

Research Methodology, Hypothesis and data variables

The main intention of this study has been conducted in the organization to estimate the effect of capital structure on financial position of the company. The analysis to be conducted with the help of indifference point approach and statistical tools like average methods, correlation and regression analysis has been selected.

Primary Data

Primary data is refers to the information or data which has been gathered directly from an organization.

Secondary Data

Secondary data is the information or data which is already gathered by some agency or institution that needs to be proceeding further. In this paper the relevant information is taken from the organization websites, financial statements and journals and magazines and some publications of the organization.

Hypothesis

The specified hypothesis is developed for this study;

H_o: The debt ratio has negative relationship among earnings per share and returns on equity.

H_a: The debt ratio has positive relationship among earnings per share and returns on equity.

The following figure shows the data variables are used for this study;

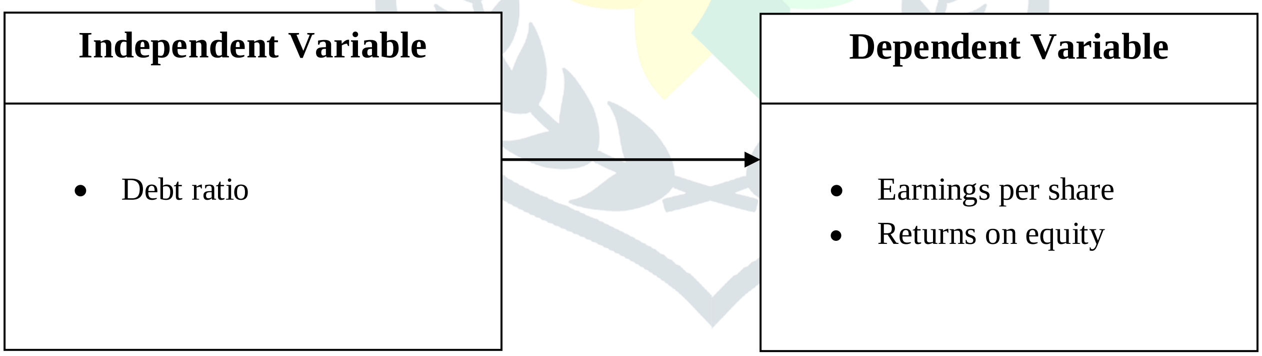


Fig. 1 variables of the study

Limitations of the Study

For this study the time period is restricted to five years & the study is analyzed based on financial data of the company.

II Review of Literature

Meaning of Capital Structure

Capital structure in common words defined as the ratio of debt, equity of a firm. In other words it defined as the share of debt in an investment of that firm. It's a vital for an organization to have a proper capital structure. The company was taking debts continuously; that company doesn't have in a position to indemnify the debts during the mentioned phase that will impact on the consideration of that company at marketplace. Hence, every organization should choose its proper capital structure with due thought to the elements referenced before.

Capital structure selection will determine weight of debt and equity and ultimately standard price of capital as well as worth of that firm. So proper capital formation was relevant in maximizing worth of that firm and minimizing the capital cost. The designed capital formation is involved whenever raising the funds in finance investment.

In continuance of the analysis based on the capital structure theories, an attempt has been made to consider various other articles and concepts to deepen the understanding and expand the research perspective.

Dr. I Satyanarayana study discussed about the impact of capital structure analysis of kesoram industries ltd from 2005-06 to 2010-11. With the help of leverage analysis they measured financial fulfillment of the company. In this study they mentioned that the company is having constant equity share capital and the company is having high debt amount compared to equity capital. The debt equity ratio provides the financial fulfillment of the company. The examination results that the debts capital has negative connection among equity capital.

Sameera Sultana and Md. Abdul Raheem Junaidi study explores the determination of capital structure at kesoram cement industries, during the period of 2005-11. They used EBIT-EPS analysis & leverage analysis for analyzing the financial fulfillment of the company. During the period the company is having constant equity share capital and the company is having higher profits due to this the company is having higher earnings per share. The study results that the company is depending on debt amount, it is not beneficial to the company. In this study they suggested that the company depends on equity rather than depends on debt.

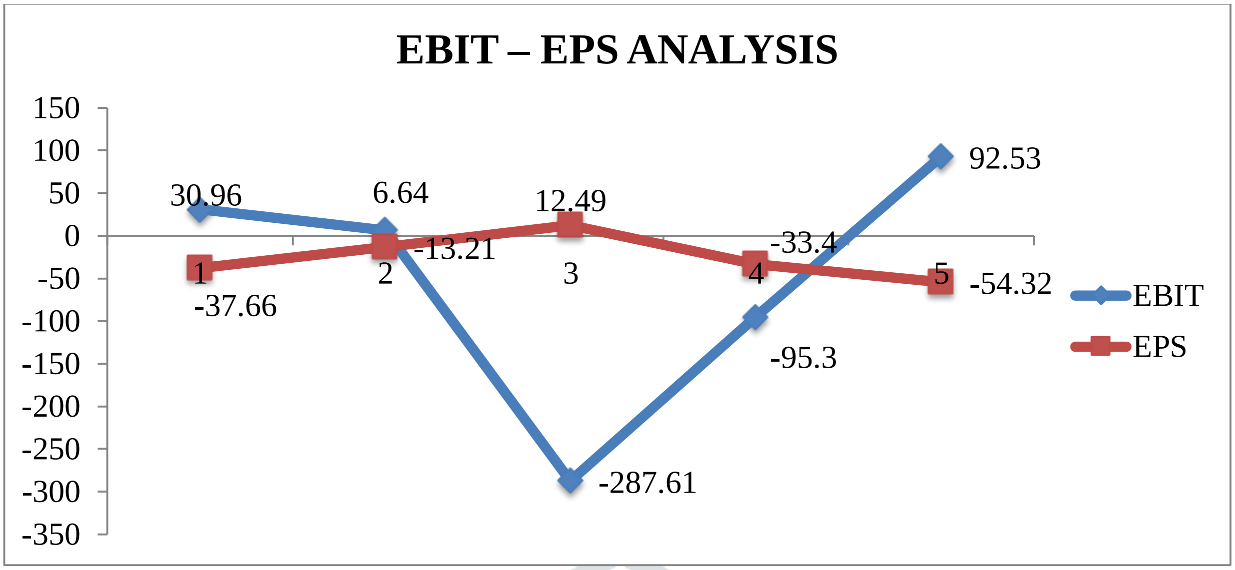
III Data Analysis & Interpretations

EBIT – EPS Analysis (Indifference point)

EBIT – EPS analysis is one of the widest tool used to decide level of debt in a company. It is also called as indifference point. Through this evaluation, assessment may be drawn for various techniques of financing by obtaining indifference factor. It's a factor to the EBIT level at which EPS remained unchanged irrespective of debt level, equity mix.

Table1: EBIT – EPS analysis

EBIT (RS. In Crores)	**EPS (RS.)**
30.96	-37.66
6.64	-13.21
-287.61	12.49
-95.3	-33.40
92.53	-54.32



This analysis shows the impact of profits before interest and taxes on income per share of a firm. Based on above analysis the EPS of a firm is positive in 3rd series and negative remaining all series. The EPS of the firm is determined on the basis of profits of that firm. The EPS of the firm becomes negative when the firm incurred losses.

Descriptive statistics

The following table shows descriptive statistics for variables. The first line of the table shows the average of the variables, including the debt ratio and earnings per share, as well as the return on equity. The respective mean values are 0.93, -25.22 and -1.22.

	Debts ratio	Earnings per share	Returns on equity
Mean	0.93	-25.22	-1.22
Median	0.94	12.49	0.34
Maximum	0.99	12.49	0.34
Minimum	0.86	-54.32	-4.20
Standard deviation	0.02	10.27	0.70

Correlation analysis

Correlation describes the quality of the relationship between the two variables. The correlation coefficient analysis was performed to determine the relationship between the company's capital structure and financial performance in this test. The below table shows the relationship between the debts ratio among returns on equity and the earnings per share of the company.

variable	Earnings per share	Returns on equity
Debts ratio	0.25	-0.64
R^2	0.063	0.410

The correlation among debt ratio and earnings per share is 0.25. The coefficient of correlation is 0.063, i.e. 6.3% variance in the capital structure is considered by the earnings per share. The correlation among debt ratio and return on equity is -0.64. The coefficient of correlation is 0.410. That is 41% variance in the capital structure is considered by the return on equity.

Regression analysis

This analysis can be used to analyze the impact of the capital structure on the company's financial performance. The below table shows the regression results used to verify the relationship between debts ratio among the earnings per share and the return on equity.

variables	Earnings per share	Returns on equity
Debts ratio	0.23	0.61
R^2	0.063	0.410
F-value	7.71	6.39
Calculated value	-62.42	1.07

From the above table it clearly observed that the calculated value is less than the table value. So accept $\mathbf{H_o}$ and reject $\mathbf{H_a}$. It means that the debts capital has negative relation among earnings per share and returns on equity.

IV Findings

From the EBIT-EPS analysis the company earns positive EPS only in 3rd series and remaining series the company earns negative EPS. From the multivariate regression analysis there is negative relations among debts ratio to earnings per share and returns on equity. It means an increase in the debt it leads to decreases the value of earnings per share and returns on equity of the company. Due to increases the debt, the company paid high interest amount it leads to decrements in the net profits of the company.

V Suggestions

This firm is getting the negative earnings per share in each series except in 3rd series, so that the firm will take appropriate actions to increase their earnings per share. Sales are decreased in every year comparing to previous year, this situation effects on profitability of this firm. The firm is having low equity share capital due to this the investors are bearing high risk. So that the firm will invite the investors to invest in this firm and to increase their equity capital so that the investors will have low risk.

VI Conclusion

After studying the capital structure, sales of kesoram cements are decreased due to this the earnings before interest and taxes decrease, it impact on the profits of the company inside the marketplace. So that company will take the new initiatives for increasing their sales so that the firms will earn maximum EPS. The firm is taking the loans heavily from banks due to this the investors is having high risk and it impacts on the liquid resources of that firm.

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