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"A STUDY OF CAPITAL STRUCTURE OF SELECTED FMCG COMPANIES IN INDIA"

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Abstract

The two principal sources of finance for a company are equity and debt. Capital structure is the mix of the various types of debt and equity capital maintained by a firm. Any firm tries to plan an optimum capital structure for itself. The optimum capital structure is one that maximises the market value of the firm Capital Structure decision is the most crucial decision for any organization. Structuring the capital of any organization in one way or other plays a major role in the growth of any company. The optimal capital structure is the one that strikes a balance between risk and return to achieve our ultimate goal of maximizing the price of the stock. A number of factors influence the capital structure decision of a company. The Financial Manager who is going to form capital structure for any particular company, be it small firm or large organization, has to look up on every little aspect very carefully. Lots of ratios, calculations have to be carefully examined before coming out with any particular output. In this study researcher has selected 5 FMCG companies to understand the capital structure policy and working capital turnover ratio of these companies.

Keywords: Capital Structure, FMCG, Financials, Ratio.

A: Introduction:-

Capital Structure of a Company refers to the composition or make up of its Capitalization and it includes all long term Capital resources i.e. loans, reserves, shares and bond. It shows the mix of a company's long-term debt, specific short-term debt, common equity and preferred equity. The capital structure is how a firm finances its overall operations and growth by using different sources of funds. In

finance, capital structure refers to the way a corporation finances its assets through some combination of equity, debt, or hybrid securities. A firm's capital structure is then the composition or 'structure' of its liabilities. For example, a firm that sells $20 billion in equity and $80 billion in debt is said to be 20% equity-financed and 80% debt-financed. The firm's ratio of debt to total financing, 80% in this example is referred to as the firm's leverage. In reality, capital structure may be highly complex and include tens of sources. Gearing Ratio is the proportion of the capital employed of the firm which come from outside of the business finance, e.g. by taking a short term loan etc. 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. Short-term debt such as working capital requirements is also considered to be part of the capital structure. A company's proportion of short and long-term debt is considered when analysing capital Structure. When people refer to capital structure they are most likely referring to a firm's debt-to-equity ratio, which provides insight into how risky a company is. Usually a company more heavily financed by debt poses greater risk, as this firm is relatively highly levered.

The long term creditors would judge the soundness of the firm on the basis of the long term financial strength measured in terms of ability to pay the interest regularly as well as repay the instalment of the principal on due dates or in one lump sum at the time of maturity. Accordingly, there are two different, but mutually dependent and interrelated, types of leverage ratio First Ratio which are based on the relationship between borrowed funds and owner’s capital. In this Paper, researcher explain the different leverage ratio as also how they can be used to draw inferences regarding the financial soundness of the firm.

B: RESEARCH OBJECTIVE:-

1. To examine the capital structure policy and pattern of selected 5 FMCG companies
2. To examine the capital employed turnover ratioof selected 5 FMCG companies
3. To examine the working capital turnover ratio of selected 5 FMCG companies

C: LITERATURE REVIEW:-

The review of literature in context to Indian corporate about the practice of capital structure are Pandey's(1984) study of 30Indian firms probes corporate managers' conceptual understanding of the cost of capital and optimum capital structure. Most of the respondents consider equity share capital as the most expensive and long-term debt as the least expensive source of finance. The low cost of debt due to tax advantage of interest and long procedures involved in the issue of equity capital led to strong preference for debt by the managers. Varma(1998) observes that at the beginning of the reform process, the Indian corporate sector was significantly over levered because of availability of subsidized institutional finance and operating risk was lower due to protected economy. The average debt to equity ratio of corporate India has reduced from 1.72:1 in 1990-91 to 1.05:1 in 1996-97. Babu and Jain (1999)

survey of 91 Indian private sector firms finds that they hold pecking order theory of capital structure. Raghunathan and Dass(1999) in their analysis of performance of Indian manufacturing sector for the period 1990 to 1999 find that the debt to equity ratio of Corporate India reached minimum of 1 in 1996 and then went up to 1.3 in1999. It was as high as 1.7 in 1990, prior to liberalization of the Indian economy. Anand's(2002) analysis of capital structure finds that the retained earnings is the most preferred source of finance followed by debt and then equity. The results seem to suggest that firms do not have specific capital structure in mind when deciding as to how best to finance their projects. Low growth firms prefer more use of debt in their capital structure vis-à-vis the high growth firms. The large firms prefer making bonds issue in the primary market. Very few firms use hybrid securities as a source of finance to protect bondholders from the firm/shareholders taking on risky or unfavourable projects. Fan and So (2000) study finds that there is strong evidence that financing and investment decisions are made simultaneously. The firms within the same industry tend to have more similar capital structure, though it is not a deliberate choice of the management. Firm size is found to be a determinant of capital structure. According to Sumit K. Majumdar, In India older firms are found to be more productive and less profitable, whereas the larger firms are conversely found to be more profitable and less productive these performance differences are explained as arising from the market restricting industrial policies that have been followed in India over the past three decades, the issue of whether larger firms are superior in performance to smaller firms, or vice versa and whether older firms is superior in performance to younger or vice versa has generated large amounts of theoretical and empirical research in the economics management and sociology discipline. An attempt has been made to introduce variables like Size, profitability, Liquidity and Interest coverage these variables are observed to be significant in explaining long term borrowing behaviour of firms.

SAMPLE SIZE

In this study, research has taken 5 FMCG companies

PERIOD OF THE STUDY

Annual reports of 5 years (2012-13 to 2016-17) have been taken under study.

D: DATA ANALYSIS:-

1. CAPITAL EMPLOYED TURNOVER RATIO-

CAPITAL EMPLOYED TURNOVER RATIO					
COMPANY	2012-13	2013-14	2014-15	2015-16	2016-17
ITC	1.26	1.20	1.12	0.84	0.85
HUL	7.07	6.49	6.61	4.37	4.32
Asian Paints	2.72	2.68	2.58	1.89	1.72
Dabur	2.27	2.16	2.01	1.53	1.24
GCPL	0.99	1.08	1.03	0.90	0.80

Capital Employed Turnover Ratio for the year 2012-13 the company maintaining the highest capital employed turnover ratio is HUL at 7.07 followed by Asian Paints at 2.72. It shows that the ability of the firm to generate maximum profits with the minimum amount of capital employed. The third position is that of Dabur at 2.27 followed by ITC at 1.26 and then GCPL at 0.99. For the year 2013-14 the company maintaining the highest capital employed turnover ratio is HUL at 6.49 followed by Asian Paints at 2.68. It shows that the ability of the firm to generate maximum profits with the minimum amount of capital employed. During year 2014-15 the company maintaining the highest capital employed turnover ratio is HUL at 6.61 followed by Asian Paints at 2.58. For the year 2015-16 the company maintaining the highest capital employed turnover ratio is HUL at 4.37 followed by Asian Paints at 1.89. It shows that the ability of the firm to generate maximum profits with the minimum amount of capital employed. The third position is that of Dabur at 1.53 followed by GCPL at 0.9 and then ITC at 0.84. In year 2016-17 the company maintaining the highest capital employed turnover ratio is HUL at 4.32 followed by Asian Paints at 1.72. It shows that the ability of the firm to generate maximum profits with the minimum amount of capital employed.

Anova: Single Factor

SUMMARY

Groups	*Count*	*Sum*	*Average*	*Variance*
ITC	5	5.27	1.054	0.03888
HUL	5	28.86	5.772	1.74412
Asian Paints	5	11.59	2.318	0.22552
Dabur	5	9.21	1.842	0.19307
GCPL	5	4.8	0.96	0.01235

ANOVA

Source of Variation	*SS*	*df*	*MS*	*F*	*P-value*	*F crit*
Between Groups	77.86602	4	19.46651	43.96349	1.23E-09	2.866081
Within Groups	8.85576	20	0.442788			
Total	86.72178	24				

INTERPRETATION-

H0 = There is no significant difference in Capital Employed Turnover Ratio between selected five companies.

H1 = There is significant difference in Capital Employed Turnover Ratio between selected five companies.

From above table for 4 and 20 degree of freedom.

Fcal is 43.96 and Ftab is 2.86.

Thus, Fcal>Ftab and p-value is less than specified α of 0.05.

So, null hypothesis is rejected and it is concluded that there is significant difference in Capital Employed Turnover Ratio between selected five companies.

2. WORKING CAPITAL TURNOVER RATIO-

WORKING CAPITAL TURNOVER RATIO					
COMPANY	2012-13	2013-14	2014-15	2015-16	2016-17
ITC	4.12	3.53	2.97	2.17	2.26
HUL	-300.57	83.91	64.08	10.79	14.57
Asian Paints	13.11	10.35	8.36	5.67	4.95
Dabur	6.27	6.54	16.30	8.53	9.16
GCPL	23.75	-10.12	-25.29	45.44	75.51

Working Capital Turnover Ratio for the year 2012-13, the company having positive working capital turnover ratios are ITC, Asian Paints, Dabur and GCPL which again reflect the efficacy of the operations of these companies. For HUL the working capital ratio for the year 2013-14 is ratio is 83.91 and that shows that the company is converting its goods produced into sales many a times during one year. Asian Paints is the company with the second highest ratio of 10.35, followed by Dabur with the value of the ratio as 6.54 and ITC with the value of 3.53. GCPL maintained a negative ratio at a value of -10.12. It shows the strength of this company in efficiently maintaining its current assets less than the current liabilities. During year 2014-15 the company having the highest working capital turnover ratio is HUL. The ratio is 64.08 and that shows that the company is converting its goods produced into sales many a times during one year. Dabur is the company with the second highest ratio of 16.3, followed by Asian Paints with the value of the ratio as 8.36 and ITC with the value of 2.97. GCPL maintained a negative ratio at a value of -25.29. It shows the strength of this company in efficiently maintaining its current assets less than the current liabilities. During year 2015-16 the working capital ratio for GCPLis 45.44 and that shows that the company is converting its goods produced into sales many a times during one year. HUL is the company with the second highest ratio of 10.79, followed by Dabur with the value of the ratio as 8.53, Asian Paints with the value of 5.67 and ITC with the value of 2.17. For year 2016-17 ratio value is 75.51 for GCPL and that shows that the company is converting its goods produced into sales many a times during one year. HUL is the company with the second highest ratio of 14.57, followed by Dabur with the value of the ratio as 9.16, Asian Paints with the value of 4.95 and ITC with the value of 2.26.

Anova: Single Factor

SUMMARY

Groups	*Count*	*Sum*	*Average*	*Variance*
ITC	5	15.05	3.01	0.69305
HUL	5	-127.22	-25.444	24645.3
Asian Paints	5	42.44	8.488	11.32622
Dabur	5	46.8	9.36	16.59825
GCPL	5	109.29	21.858	1670.938

ANOVA

Source of Variation	*SS*	*df*	*MS*	*F*	*P-value*	*F crit*
Between Groups	6171.104	4	1542.776	0.292804	0.879169	2.866081
Within Groups	105379.4	20	5268.97			
Total	111550.5	24				

INTERPRETATION-

H0 = There is no significant difference in Working Capital Turnover Ratio between selected five companies.

H1 = There is significant difference in Working Capital Turnover Ratio between selected five companies.

From above table for 4 and 20 degree of freedom.

Fcal is 0.29 and Ftab is 2.86.

Thus, Fcal<Ftab and p-value is greater than specified α of 0.05.

So, null hypothesis is accepted and it is concluded that there is no significant difference in Working Capital Turnover Ratio between selected five companies.

E: CONCLUSION:-

Working capital is the lifeline of every industry, irrespective of whether it's a manufacturing industry or service industry. Working capital is the prime and most important requirement for carrying out the day to day operations of the FMCG business. Working capital gives the much-needed liquidity to the FMCG industry. Working capital finance reduces the overall fund requirement, required to build up the current assets, which in turn help to improve turnover ratio of the company.

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