



A Study on Capital Structure and Financial Performance of Selected Textile Companies in India

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ABSTRACT

In this paper an attempt to identify the impact between Capital structure and financial performance of selected textile companies, for accomplishment of the objective, the data collected from the annual reports for ten years. The collected data is analyzed and computed to fit for drawing inferences; this study utilizes various ratios, correlation and compounded growth rate. The results reveals that there exists a negative relationship between capital structure and financial performances. It is reflect the insignificant level of the selected textile companies in India. Hence Business companies mostly depend on the debt capital. Therefore, they have to pay interest expenses much.

Keywords : Capital Structure, Financial Performance, Profitability Ratios, Correlation.

Introduction

Capital is the life blood and nerve center of a business. It is very essential for the smooth running of any business. Capital structure is closed link with corporate financial performance. Financial performance (reflected in profit maximization, maximizing return on assets and maximizing shareholder return) is based on the firm's efficiency. Financial Performance is the blue print of the financial affairs of a concern and reveals how a business has prospered under the competitive environment.

The Indian textile industry is the second largest in the world second only to china. India earns about 30 per cent of its total foreign exchange through textile exports. Further, it also contributes nearly 14 per cent of the total industrial production and around 3 per cent to the GDP (Gross Domestic Product) of the country. Today, the Indian textile industry employs around 35 million personnel directly and it accounts for 21 per cent of the total employment generated in the economy. Thus, much of India's economic growth is largely dependent on the textile manufacturing and exports. Financial Performance is the blue print of the financial affairs of a concern and it reveals the organization's ability to translate its financial resources into mission related activities.

Statement of Problem

In reality, capital structure of a firm is difficult to determine. Financial managers are difficult to exactly determine the optimal capital structure. A firm has to issue various securities in a countless mixture to come across particular combinations that can maximum its overall value which means optimal capital structure. If a wrong mix of finance is employed; the performance and survival of the business enterprise may be seriously affected. Survival and growth needs resources but financing of these resources has limitation. Therefore, the present study is undertaken to know the impact of capital structure on financial performance of selected textile companies in Indian

Objectives of the study

- To analyze the financial performance of the selected textile companies.
- To examine the capital structure of selected textile com-

panies.

- To measure the impact of capital structure on financial performance.
- To offer suggestions for the improvement of textile companies in India.

Research methodology

To produce the above mentioned research objective, the data for this study was gathered from Prowess' corporate databases developed by CMIE (Centre for Monitoring Indian Economy) and from other journals, books magazine. Ten companies (Aditya Birla Nuvo Ltd (C₁), Arvind Ltd (C₂), Ginni Filaments Ltd (C₃), Grasim Industries Ltd (C₄), Himatsingka Seide Ltd (C₅), Indo Rama Synthetics (India) Ltd (C₆), Maharaja Shree Umaid Mills Ltd (C₇), Nahar Spinning Mills Ltd (C₈), Page Industries Ltd (C₉) and Ruby Mills Ltd (C₁₀)) are taken for the study representing the period of 2002-03 to 2011-12. The statistical tool used in the analysis of data is Ratio Analysis, Correlation Analysis, Trend Analysis, Compound Growth Rate Analysis and Path Analysis. To identify the variable associated with capital structure correlation analysis is employed Debt Equity Ratio (DER) is used as dependent variable and Operating Profit Margin (OPM), Net Profit Margin (NPM), Return on Investment (ROI), Return on Asset (ROA), Return on Equity (ROE) and Earning Per Share (EPS) used as independent variable.

Limitations

- The study carries all the limitations inherent with the secondary data and financial information.
- The study is restricted to selected companies only for the period of ten years.
- Various accounting and statistical tools extensively used for the study have their own incidental limitations.

Review of literature

Toraman, Cengiz and Kilic, Yunus and Gul Reis, Sukriye (2013) The capital structure decisions of firms have a crucial importance on firms' financial performance. The capital structure concept is generally described as the combination of debt and equity that make the total capital of firms. The profitability of an enterprise is directly affected by capital structure

decision The aim of this study is to investigate the effects of capital structure decisions on firms' profitability in manufacturing sector in Turkey. The regression analysis was employed by using financial ratios obtained from financial statements of firms within the scope of analysis. The result shows that the capital structure has significant influence on firm performance have been determined and general assessment has been made.

Table 1
Table Showing the DER

Company	Average	SD	CV	Skewness	Kurtosis
C1	0.65	0.27	42.18	-0.16	-0.73
C2	1.25	0.22	17.53	0.25	1.3
C3	2.9	1.3	44.84	0.47	-0.83
C4	0.37	0.2	55.61	-0.13	-0.82
C5	0.49	0.39	79.67	-0.08	-2.05
C6	1.33	0.42	31.83	0.16	-1.81
C7	0.79	0.41	51.58	0.57	0.38
C8	1.14	0.7	61.78	0.15	-1.5
C9	0.99	0.65	65.5	0.8	-1.04
C10	2.21	1.4	63.57	0.19	-1.73
	1.21				

It is inferred that among the ten companies half of the companies namely Arvind Ltd, Ginni Filaments Ltd, Indo Rama Synthetics (India) Ltd, Nahar Spinning Mills Ltd and Ruby Mills Ltd have high equity share capital and remaining half have low equity share capital. It is observed that debt equity ratio is normally distributed.

Table 2
Table Showing the OPM

Company	Average	SD	CV	Skewness	Kurtosis
C ₁	15.87	2.4	15.15	-0.81	-0.52
C ₂	21.95	5.9	26.89	-0.15	-1.89
C ₃	10.95	5.9	53.9	-1.04	-0.87
C ₄	30.75	6.62	21.53	0.01	-0.94
C ₅	29.63	18.27	61.68	-0.04	-2.32
C ₆	12.61	6.07	48.08	1.02	0.1
C ₇	27.39	36.55	133.47	2.68	7.35
C ₈	15.72	6.15	39.15	-1.57	2.5
C ₉	18.91	4.34	22.97	-1.02	-0.55
C ₁₀	34.84	20.32	58.31	1.29	0.64
	21.86				

From the above table it is understood that average operating profit margin ranges between 10.95 (C₃) and 34.84 (C₁₀) and the overall average value is 21.86. The highest coefficient of variation was found in C₇ (133.47). Four companies are positively skewed and remaining six are negatively skewed. Among the ten companies the kurtosis of six companies indicates leptokurtic distribution and four companies indicate platykurtic distribution.

Table 3
Table Showing the NPM

Company	Average	SD	CV	Skewness	Kurtosis
C ₁	6.09	1.61	26.51	-0.74	0.8
C ₂	5.67	4.2	74	-0.42	0.09
C ₃	-0.63	4.27	-682.76	-1	-0.94
C ₄	17.95	5.93	33.04	-0.08	-1.04
C ₅	14.43	20.36	141.11	-0.12	-2.26
C ₆	2.75	4.06	147.44	0.39	0.42
C ₇	16.59	29.71	179.05	2.62	7
C ₈	3.61	4.8	132.8	-1.36	1.49
C ₉	10.55	2.73	25.88	-1.09	-0.4
C ₁₀	14.29	13.5	94.5	1.49	1.16
	9.13				

From the above table it is understood that average net profit margin ranges between -0.63 (C₃) and 17.95 (C₄) and the overall average value is 9.13. The highest coefficient of variation was found in C₇ (179.05). Three companies are positively skewed and remaining seven are negatively skewed. Among the ten companies the kurtosis of four companies indicates leptokurtic distribution and six companies indicate platykurtic distribution.

Table 4
Table Showing the ROI

Company	Average	SD	CV	Skewness	Kurtosis
C ₁	7.2	1.97	27.41	-0.38	0.59
C ₂	7.77	6.7	86.14	0.36	1.79
C ₃	-6.73	22.53	-334.57	-1.42	0.81
C ₄	19.79	5.94	30.01	0.34	-1.15
C ₅	5.5	9.65	175.52	-0.07	-1.52
C ₆	7.85	13.14	167.34	-0.56	0.76
C ₇	20.48	18.86	92.08	1.31	0.8
C ₈	3.45	10.57	305.88	-1.35	3.34
C ₉	54.74	25.03	45.73	0.89	-0.02
C ₁₀	17.28	10.22	59.17	0.81	0.26
	13.73				

From the above table it is understood that average ROI ranges between -6.73 (C₃) and 54.74 (C₉) and the overall average value is 13.73. The highest coefficient of variation was found in C₈ (305.88). Partial companies are positively skewed and partial companies are negatively skewed. Among the ten companies the kurtosis of three companies indicates leptokurtic distribution and seven companies indicate platykurtic distribution.

Table 5
Table Showing the ROA

Company	Average	SD	CV	Skewness	Kurtosis
C ₁	0.05	0.02	42.09	0.42	-0.48
C ₂	0.04	0.03	90.94	1.03	2.96
C ₃	-0.01	0.04	-609.32	-1.18	0
C ₄	0.15	0.05	33.79	1.07	1.95
C ₅	0.05	0.08	149.86	0.33	-1.51
C ₆	0.04	0.06	141.83	-0.21	0.02
C ₇	0.14	0.15	113.27	1.72	2.24
C ₈	0.02	0.04	186	-1.5	2.62
C ₉	0.27	0.08	29.84	1.38	1.57
C ₁₀	0.05	0.02	43.41	0.6	0.18
	0.08				

From the above table it is understood that average ROA ranges between -0.01 (C₃) and 0.27 (C₉) and the overall average value is 0.08. The highest coefficient of variation was found in C₅ (149.86). Seven companies are positively skewed and remaining three is negatively skewed. Among the ten companies the kurtosis of two companies indicates leptokurtic distribution and eight companies indicate platykurtic distribution.

Table 6
Table Showing the ROE

Company	Average	SD	CV	Skewness	Kurtosis
C ₁	245.26	62.9	25.65	-0.17	-1.11
C ₂	54.27	50.15	92.42	1.14	3.27
C ₃	-6.42	30.57	-476.22	-1.09	-0.3
C ₄	1392.15	650.48	46.73	0.32	-0.72
C ₅	77.97	129.48	166.06	0.21	-1.46
C ₆	38.75	56.22	145.09	-0.09	0.12
C ₇	464.8	646.27	139.04	1.73	1.43
C ₈	122.22	339.75	277.97	-1.01	3.1

C ₉	332.18	213.51	64.27	1.36	1.58
C ₁₀	259.45	713.7	275.08	2.79	8.5
	298.06				

From the above table it is understood that average ROE ranges between -6.42 (C₃) and 1392.15 (C₄) and the overall average value is 298.06. The highest coefficient of variation was found in C₈ (277.97). Six companies are positively skewed and remaining four is negatively skewed. Among the ten companies the kurtosis of four companies indicates leptokurtic distribution and six companies indicate platykurtic distribution.

Table 7
Table Showing the EPS

Company	Average	SD	CV	Skewness	Kurtosis
C ₁	23.88	6.21	25.99	-0.14	-1.14
C ₂	5.44	4.64	85.37	1.71	4.4
C ₃	0.77	0.83	107.61	1.28	1.53
C ₄	136.46	64	46.9	0.31	-0.7
C ₅	8.07	10.33	128.03	0.97	-1.06
C ₆	4.26	4.44	104.25	0.84	-0.64
C ₇	46.05	64.41	139.86	1.73	1.43
C ₈	12.29	10	81.34	0.69	1.11
C ₉	112.65	130.44	115.79	2.01	4.5
C ₁₀	44.08	51.18	116.1	1.49	0.77
	39.4				

From the above table it is understood that average EPS ranges between 0.77 (C₃) and 136.46 (C₄) and the overall average value is 39.4. The highest coefficient of variation was found in C₇ (139.86). Nine companies are positively skewed and remaining one is negatively skewed. Among the ten companies the kurtosis of three companies indicates leptokurtic distribution and seven companies indicate platykurtic distribution.

Table 8
Table showing Correlation Analysis of Variables associated with Capital Structure

Variables	R	r ²
OPM	0.162	0.026
NPM	-0.278**	0.077
ROI	-0.254*	0.064
ROA	-0.388**	0.151
ROE	-0.316**	0.100
EPS	0.126	0.016

** Significant at one per cent level
at five per cent level

*Significant

Out of six variables selected, two variables namely OPM and EPS are positively correlated and remaining four variables namely NPM, ROI, ROA and ROE are negatively correlated. NPM, ROA and ROE are significant at one per cent level and ROI is significant at five per cent level. The coefficient of variation explains 15.1 per cent of variation in DER is due to ROA.

Findings

Correlation analysis explains, there is a weak positive relationship between operating profit margin and capital structure (0.162) at the same time, there is a negative relationship between net profit margin, return on investment, return on asset, return on equity and earnings per share and capital structure. It is focused on the overall point of view of the relationship between the capital structure and financial performance is insignificant. It is reflect the insignificant level of the selected textile companies in India. Selected textile companies mostly depend on the debt capital. Therefore, they have to pay interest expenses much.

Suggestion

It is suggested that the financial analysts and managers should emphasize on the optimum level of capital structure and efficient utilization and allocation of resources in order to increase the Company's financial performance based on capital structure.

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