ISSN NO. 2320-5407

Journal homepage: http://www.journalijar.com

INTERNATIONAL JOURNAL OF ADVANCED RESEARCH

RESEARCH ARTICLE

FINANCING DECISIONS: A CASE STUDY OF SELECTED CEMENT COMPANIES OF INDIA

[*] MANJUNATH. S. AWALAKKI

Assistant professor, Visvesvaraya Technological University, Post Graduate Center, Kalaburagi, Karnataka, India,

Manuscript Info

Manuscript History:

Received: 12 June 2015
Final Accepted: 26 July 2015
Published Online: August 2015

Key words:

BUSINESS RISK, CAPITAL STRUCTURE, FINANCIAL RISK, LEVERAGE, MARKET VALUE

***Corresponding Author**

MANJUNATH S. AWALAKKI

Abstract

Since, last two decades of Indian economy, there is a continues research on company financing activities, particularly aimed at understanding how companies finance their investments and what source they used to finance. In practice, it is observed that finance managers use different combinations of debt and equity to meet the various financial requirements of the company at least cost, and risk and for the long term benefit of the company. Therefore, this study is aimed to make analyse of capital structures pattern of various companies for the period of 2008-09 to 2013-14 and analyse the effect of changes in capital structure on its investment pattern over the period of time. This study also attempts to make an intra-company analysis with the objective to determine the importance of debt-equity mix for the effective investment policy. Similarly, To study the financing decisions, this paper includes the trend analysis for analyzing the detail financial information of five most reputed cement companies, that are, ACC cement Ltd, Ultratech cement Ltd, Ambuja Cement, J.K. Cement, and Chettinad cement for the period of five year i;e 2008-09 to 2013-14.

INTRODUCTION

Financing decisions are one of the most critical areas and the challenging job for the finance managers, because, (Bhat, 1994) It has direct impact on the financial performance and capital structure of the companies. The finance manager of every company is always looking to maximize the economic welfare of the owners as represented by the market value of the firm. For this purpose, he has to take number of decisions like investment, financing and dividend decisions. The financing decision is mainly involves two choices. The first is the dividend choice – the distribution of retained earnings to be ploughed back and to be paid out as dividends. The second is a choice of capital structure – the proportion of external finance to be borrowed and the proportion to be raised in the form of new equity. In real sense, the decisions about both the choice should not impact on the value of the firm. Because these decisions are related to either the form of distribution, type of security, or make up of the ownership structure, but not to the investment decision. Generally, the firms have the internal and external sources of fund in its capital structure to finance their investments. Internal sources include retained earnings and depreciation; whereas the external sources consist of new borrowings or the issue of shares.

(Gupta, 2011) Capital structure decisions have great impact on the firm’s financial performance. Exactly how firms choose the amount of debt and equity in their capital structures remains an enigma. Capital structure is the combination of debt and equity that finance the organization's strategic plan. (M.R, 2010) The effective management of capital structure ensures the availability of required fund to finance the future growth and enhance the financial performance. The debt equity relationship is depends upon the nature of industries involved like company's line of business and its development. A company is said to be highly leveraged, if it includes the maximum debt source of finance in its capital structure, which results, the company find its freedom of action restricted by its creditors and may have its profitability affected with the payment of high interest costs. There is a significant difference between the industry and the individual companies within an industry in terms of capital structure. There are number of factors influencing the capital structure decision of the company, but the judgment of the person making the capital structure decision plays a crucial part. Two similar companies can have different capital structures as per the different judgement of decision makers with the significance of various factors. Thus, the financing decisions have no effect on firm value, as it is the residue of the more important investment decisions. Similarly, this paper is an attempt to determining the impact of variations in the capital structures of various cement companies on their investment pattern over the period of time and highlighting the importance of debt capital and equity capital to determining the value of investments of the companies.

REVIEW OF LITERATURE

(Jackling, 2009) The ownership of family firms was frequently associated with pyramiding, family trusts and cross holding. These structures increased the divergence of control and cash flow rights presenting special agency problems associated with corporate governance. (Rouf, 2015) Investigates the impact of capital structure choice on performance of 64 firms from 1997-2005 in the Bangladesh capital market. He employs three accounting –based measures including ROA, ROE and gross profit margin, and concludes capital structure choices, generally, has a weak –to- no impact on firm performance. (Myers, 1984) He stated that there is not sufficient evidence on the relationship between risk and capital structure. According to the trade-off theory, higher debt ratio increases the probability of financial distress. The firm’s debt ratio is affected with the positive financial distress/bankruptcy costs. (Pratheepkanth, 2011)**.** He analyzed the capital structure and its impact on financial performance capacity during 2005 to 2009 of Business companies in Sri Lanka. The results shown the relationship between the capital structure and financial performance is negative. (Sudesh kumar, 2012) The capital structure decision of the pharmaceutical companies has very little effect on its investment pattern, which defines that the company is using long term sources of funds to finance its current assets and its operational activities of its business with the object to attain the long term solvency and maximizing profitability with least cost of capital. (Siberman, 1977) He concluded that, if lower the degree of financial leverage adopted then higher will be the variability in rate of return on invested capital. Hence, the ultimate determinant of leverage would be the variance, not the rate of return

RESEARCH METHODOLOGY

This study is based on the secondary data i; e financial information from the company’s annual reports. The study is focused on determining the capital structure pattern of the companies and its impact on the investment pattern over the period of time. To achieve the set objectives of the study the financial analysis technique is applied i; e Trend Analysis on the company’s financial statements for the period of 2008-2013 to analyse the change in capital structure and its impact on investment pattern of the companies. The sample size of the study is consist of five most growing cement companies that are Acc cement Ltd, Ultratech cement Ltd, Ambuja cement, J.K. cement, and Chettinad cement.

OBJECTIVES OF THE STUDY

1. To determine the capital structure pattern of the cement companies for the period of 2008-09 to 2013-14.
2. To analyse the impact of change in capital structure on the investment pattern of the firms.
3. To analyse the intra-company’s capital structure and
4. To determine the relationship of change in capital structure with the company’s investment policy.

ANALYSIS OF THE STUDY

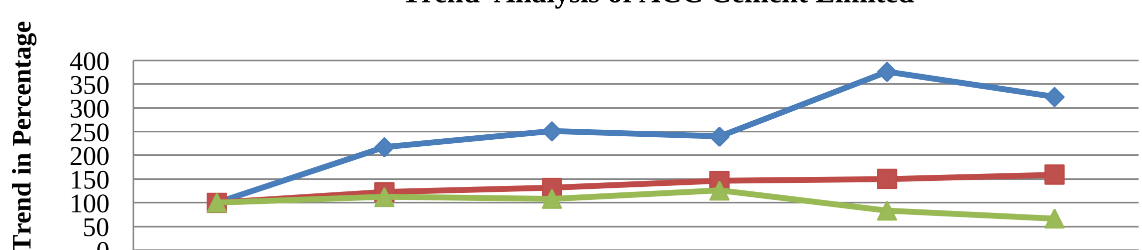
ACC Ltd.,

ACC (ACC Limited) is India's foremost manufacturer of cement and concrete. ACC's operations are spread throughout the country with 17 modern cement factories, more than 50 Ready mix concrete plants, 21 sales offices, and several zonal offices. It has a workforce of about 9,000 persons and a countrywide distribution network of over 9,000 dealers. Since inception in 1936, the company has been a trendsetter and important benchmark for the cement industry in many areas of cement and concrete technology. The ACC has poised to grow in the long term ACC Ltd. is India’s oldest and second largest cement company with a total capacity of about 23.86 Million tons in 2013. It commands a market share of 11 compared to 18.3%of Ultratech Cements and 9.6% of Ambuja Cements. It recently commissioned the world’s largest cement kiln with 12500TPD capacity. It was acquired in 2005 by Holcim Ltd – one of the world’s leading suppliers of cement. Therefore to study the objective of the study, the trend analysis is made on the basis financial statements for the period 2008-09 to 2013-14.

As per the data available in Table - 1, it is clear that the ACC Ltd. is using the debt and equity source of finance in its capital structure. The trend analysis of the company’s financial performance states that there is a consistent growth in the use of equity financing. So therefore the growth of equity financing of the company in 2013-14 is 149.81% as compare to the base year of the study i;e 2008-09 Similarly, the analysis states that company is looking to be keen towards increasing the stake of the equity shareholders to achieve the company's overall growth On the other hand, the trend in company's debt financing is looking to be very uncertain or fluctuating. As per the above analysis, in 2011-12 there is a increase in use of debt capital as compare to the previous year, but in 2008-09 there is fair growth in debt financing, which is more than 1.2 time as compare to the base year, from 2012-13 there is decrease in the debt financing. Similarly with analysis, it seems that the company's capital structure policy is fair effective, because the company is using minimum fixed cost source of funds, which ultimately affect the company's profitability and increase the financial aid on it. The analysis to measure the effect of change in capital structure on the company's investment pattern states that there is a growth in the investment pattern at a consistent rate over the period of time under study but at 2011-12 there is slit shift from consistent level. But in overall the growth rate of the company's investments is more than 323.08 % in the 2013-14 as compare to the base year 2008-09. But, the comparison of growth of company's investment pattern to growth of capital structure, make it clear that the change in company's capital structure has a very fair impact on its investment pattern, because the percentage change in capital structure

Table-1: GROWTH ANALYSIS OF ACC LIMITED (Amount in crores)

Year	Shareholder's Fund	Trend	Debt	Trend	Total Investment	Trend
2008-09	4,928	100.00	818.00	100.00	679.080	100.00
2009-10	6,016	122.07	916.00	111.98	1,475.64	217.23
2010-11	6,469	131.27	886.00	108.31	1,702.67	250.64
2011-12	7,192	145.94	1029.00	125.79	1,624.95	239.28
2012-13	7,383	149.81	680.00	83.12	2,553.55	376.03
2013-14	7,825	158.78	542.00	66.25	2,194.02	323.08



	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14
Investment	100	217.23	250.64	239.28	376.03	323.08
Equity	100	122.07	131.27	145.94	149.81	158.78
Debt	100	111.98	108.31	125.79	83.12	66.25

Figure-1: (TREND ANALYSIS OF ACC CEMENT LIMITED)

amount is less than the percentage change in investment during the period of study. Therefore, it can be said that the company is using the long term source of funds to finance its current assets also along with the long-term investment to sustain the company's profitability at the least cost of capital.

Ultratech Cement Limited

Ultratech Cement Ltd. is the largest manufacturer of grey cement, Ready Mix Concrete (RMC) and white cement in India. It is also one of the leading cement producers globally. The company has an installed capacity of [10]64 Million

Tonnes Per Annum (MTPA) of grey cement. Ultratech Cement has 12 integrated plants, 1 clinkerisation plant, 16 grinding units and 6 bulk terminals. Its operations span across India, UAE, Bahrain, Bangladesh and Sri Lanka. The Trend analysis of the company for the year 2008-09 to 2013-14 is as follow. As per the data available in Table - 1, it is clear that the Ultratech cement limited is using the debt and equity source of finance in its capital structure. The trend analysis of the company's financial performance states that there is a consistent growth in the use of equity financing. So therefore the growth of equity financing of the company in 2013-14 is 474.68% as compare to the base year of the study i; e 2008-09. Similarly, the analysis states that company is looking to be keen towards increasing the stake of the equity shareholders to achieve the company's overall growth.

Table-2 GROWTH ANALYSIS OF ULTRTECH CEMENT * (amount in crores)

Year	Shareholders fund	Trend	Debt	Trend	Total Investment	Trend
2008-09	3,602	100.00	2142	100.00	1,035	100.00
2009-10	4,609	127.95	1605	74.92	1,670	161.35
2010-11	10,666	296.11	4145	193.5	3,730	360.38
2011-12	12,860	357.02	4153	193.88	3,789	366.08
2012-13	15,235	422.95	5409	252.52	5,109	493.62
2013-14	17,098	474.68	5199	242.71	5,392	520.96

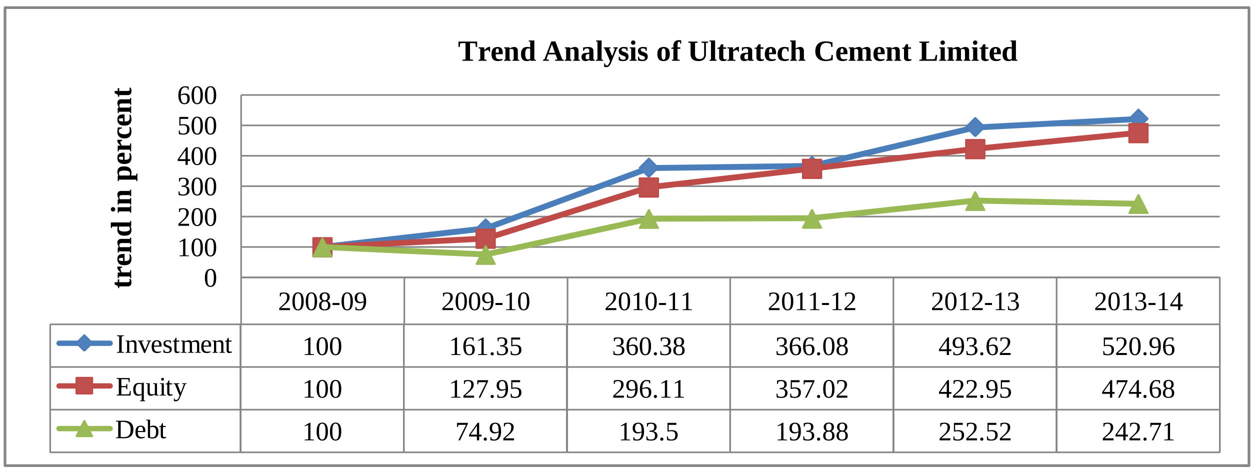


Figure 2 (TREND ANALYSIS OF ULTRATECH CEMENT LIMITED)

On the other hand; the trend in company's debt financing is looking to be very uncertain or fluctuating. As per the above analysis, in 2008-09 there is a decrease in use of debt capital as compare to the previous year, but in 2010-11 there is 258.27 % growth in debt financing, which is more than 1.93. times as compare to the base year, again in 2011-12 there is small increase and after that in 2012-13, company raise debt capital at level, which can be assumed to be the maximum level of period under study i;e 2.52 time more as compare to the base year. Similarly with analysis, it seems that the company's capital structure policy is effective, because the company is using minimum fixed cost source of funds, as compared with equity fund, which ultimately affect the company's profitability and minimize the financial burden on it. The analysis to measure the effect of change in capital structure on the company's investment pattern states that there is a growth in the investment pattern at a consistent rate over the period of time under study. But in overall the growth rate of the company's investments are more than 520.96 in the 2013-14 as compare to the base year 2008-09. But, the comparison of growth of company's investment pattern to growth of capital structure, make it clear that the change in company's capital structure has a very better impact on its investment pattern, because the percentage change in capital structure amount is more than the percentage change in investment during the period of

* Shareholders fund is total net worth of the company

study. Therefore, it can be said that the company is using the long term source of funds to finance its current assets also along with the long-term investment to sustain the company's profitability at the least cost of capital.

Ambuja Cement Limited

Formerly known as Gujarat Ambuja Cements Limited, Ambuja Cements Ltd, a part of a global conglomerate Holcim, is one of India's leading cement manufacturers and has completed over 25 years of operations. The company, initially called Gujarat Ambuja Cements Ltd, was founded by Narotam Sekhsaria in 1983 in partnership with Suresh Neotia. Global cement major Holcim acquired management control of Ambuja in 2006. Ambuja has grown dynamically over the past decade. Its current cement capacity is 28.75 million tons.

Table-3 GROWTH ANALYSIS OF AMBUJA CEMENT (amount in crores)

Year	Shareholders fund	Trend	Debt	Trend	Total Investment	Trend
2008-09	5,672. 87	100.00	288.67	100.00	332.39	100.00
2009-10	6,470.90	114.06	165.70	57.40	727.01	218.72
2010-11	7,330.10	129.21	65.03	22.52	625.95	188.31
2011-12	8,069.44	142.24	49.36	17.09	864.31	260.02
2012-13	8,805.06	155.21	34.63	11.99	1655.83	498.15
2013-14	9,485.54	167.20	29.15	10.09	1788.45	538.05

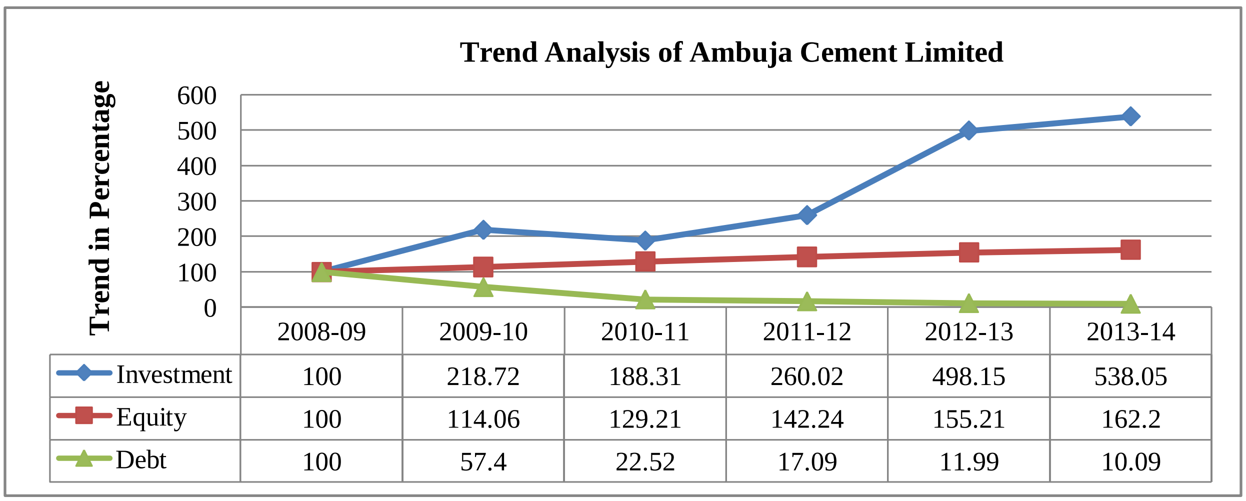


Figure-3 (TREND ANALYSIS OF AMBUJA CEMENT LIMITED)

J.K. Cement Limited

J.K. Cement Ltd is an affiliate of the multi-disciplinary industrial conglomerate J.K. Organisation which was founded by Lala Kamlapat Singhania. For over four decades, J.K. Cement production at our first grey cement plant at Nimbahera in the state of Rajasthan in May 1975. Subsequently the Company also set up 2 more units in Rajasthan at Mangrol and Gotan. In the year 2009 the company extended its footprint by setting. Today J.K. Cement has an installed grey cement capacity of 10.5 MTPA making it one of the leading manufacturers in the country. The Trend analysis of the company for the year 2008-09 to 2013-14 is as follow.

Table-4 GROWTH ANALYSIS OF J.K. CEMENT (amount in crores)

Year	Shareholders fund	Trend	Debt	Trend	Total Investment	Trend
2008-09	1186. 05	100.00	564. 40	100.00	10.74,08	100.00

2009-10	1353. 74	114.13	1073.72	190.24	5.98,80	55.67
2010-11	1387. 03	116.96	1384.11	245.23	5.84,19	54.37
2011-12	1529. 00	128.91	1396.49	247.42	10.84,19	100.93
2012-13	1697. 38	143.11	1141.79	202.30	169.29,88	1576.16
2013-14	1758. 46	148.26	2185.05	387.14	299.5066	2788.64

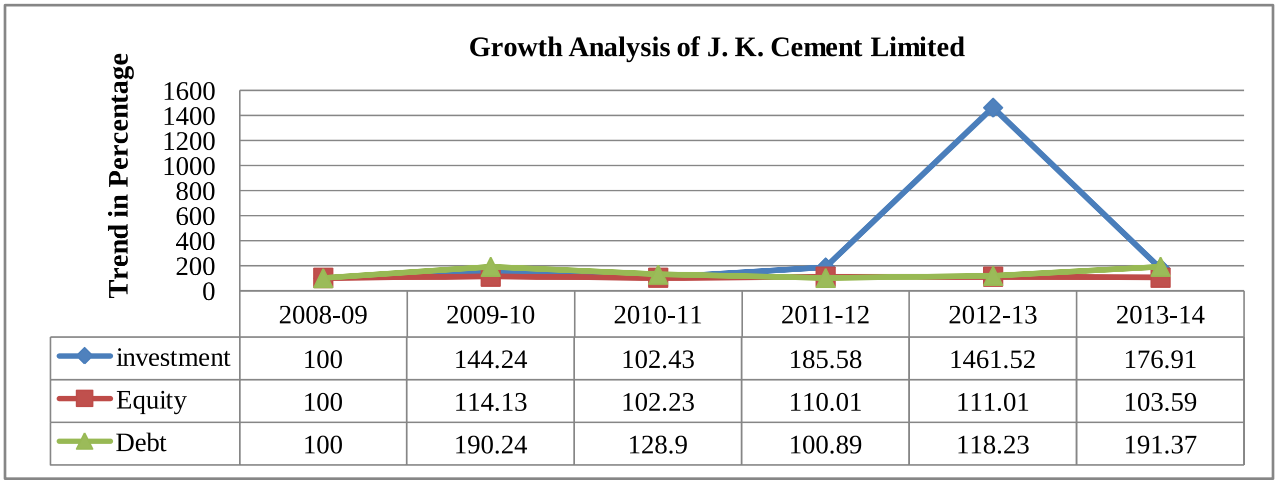


Figure-4 (TREND ANALYSIS OF J.K. CEMENT LIMITED)

The J.K Cement is using the debt and equity source of finance in its capital structure. As per the analysis of the study, there is a growing trend in the company's equity financing at consistent rate in the initial years but after from 2008-09 to 2013-14 is 100% to 148.26 %. On the other hand, the trend in debt financing is increasing in the initial four years till 2011-12, but after that it decrease in later period of the study, which states the decreasing trust of the company to raise the funds from debt sources at last year it regained the trust of the company to raise the debt. Similarly, in the above figure, it clear that after the half of the period of study there is fluctuating trend in debt financing of the company capital structure, which ultimately states the fluctuations in company's financial burden due to the fluctuations in the fixed cost bearing debt sources. As per the objective of the study to measure the impact of change in company's capital structure on the company's investment pattern, the analysis of the study states that the company is increasing its investment value every year but at the , 2010-11 the investment value was little less as compared to last year's (2009-10) investment value in terms of 2.33%, but after that there is gigantic increase in the investment value from base year(2008-09) to 2013-14 from 100% to 2788.64% a 26 times more as compared to base year investment. Whereas it seems that such a fair variation in the company's capital structure has a very stupendous impact in the company's investment pattern. Because, the effect on investment pattern due to the increasing in company's debt financing and sudden change in debt financing has mostly offset by the increase in equity financing over the period of time. In spite of such fair variation in the company's capital structure, the overall trend in capital of the company is increasing, but not as compared to the increasing rate of the company's investments. Therefore, it can be said that the company is using it long term sources of funds especially from equity to finance its current assets along with the object to sustain the solvency & profitability at the least cost of capital.

Chettinad cement limited

Chettinad cement is operating its cement business spanning three generations. Since its establishment in 1962 with wet process cement plant at Puliyur near Karur. The Milestone and achievement of Chettinad cement are 0.4 MTPA cement production capacity with wet process plant installed at Puliyur in 1969, Work is under progress for a new Green field production line of 2.5 MTPA cement with 1 No. of 30MW Coal based captive power plant in Kallur Village, Chincholi Taluk and Gulburga Dist of Karnataka state and expected to be commissioned in year. The trend analysis of the company's capital structure and its impact on the investment pattern for the period under study is as under: As per the analysis of the study the capital structure of the company is consisting of equity capital and debt capital. The trend analysis used under study states that the company is liberal fluctuating policy to its equity financing over the period of time, which is found to be more than 6% till end of the period under study 2013-14; On the other hand, the trend in using the debt financing is decreasing during the time period, from 2008-09 to 2013-14 is 100% to 86.85%. Which states that the company is using the liberal policy regarding the use of debt financing and the trend of using debt finance is looking to be very uncertain, Similarly, to study the influence of change in capital structure pattern on the company's investment pattern, the trend used by company to make the use of long term source of fund for the long term investment is studied.

Table-4 GROWTH ANALYSIS OF CHETTINAD CEMENT (amount in crores)

Year	Shareholders fund	Trend	Debt	Trend	Total Investment	Trend
2008-09	355.15	100.00	997. 03	100.00	0.58	100.00
2009-10	863. 72	243.19	758.87	123.88	0.58	00.00
2010-11	925.71	107.17	896.06	118.07	0.58	00.00
2011-12	1080. 41	116.71	989.28	110.40	0.58	00.00
2012-13	1195. 60	110.66	884.06	89.36	0.00	00.00
2013-14	1,278.50	106.93	767.88	86.85	0.00	00.00

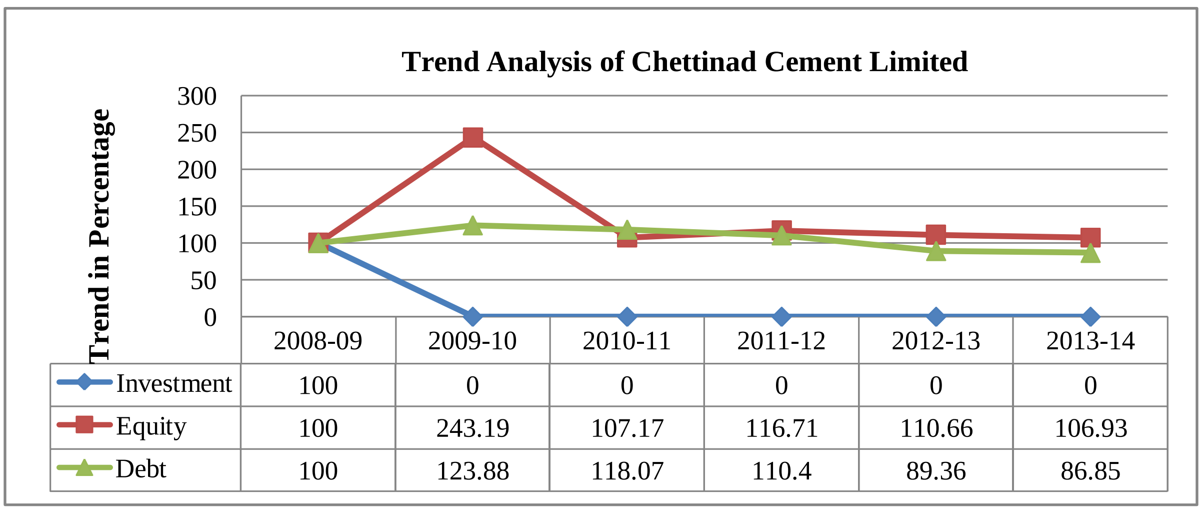


Figure-5 (TREND ANALYSIS OF CHETTINAD CEMENT LIMITED)

The analysis states that there is a negative growth rate in the investments, which is more than -0.58 % in the end of year as compare to the base year under study. But, such condition of investment is not comparable to the fluctuation growth in fund from different long term source. In spite of maximum fluctuation growth in the equity financing pattern over the period of time with consistent decline of debt financing, the growth trend in investment is negative growth downward. Such an unequal match of growth penlight the company's financing policy for using the long term source of funds to finance its current assets and to maintain the long term assets and investments over the period of time. As per the analysis, it is clear that company is using the minimum fixed cost bearing source of finance as compare to the fluctuation equity finance, which may ultimately to be a financial relief on the company, but it can also be assumed that the company is using the fluctuating long term source of funds that may hinder the growth and profitability, it the case investment pattern of the company is in negative growth.

TO SUM UP

The overall analysis of the study states that the capital structure of all the companies is consisting of equity funds and debt funds As far as the equity capital is concern, the ACC Ltd and Ultra Tech both of the companies are increasing their equity capital every year at a consistent growth rate, whereas the Ultratech cement ltd made the tremendous growth in the equity financing over the period of time under study. In Ultratech cement, the growth rate of equity financing in the end of the period under study is double than the growth rate of debt financing. Similarly, in case of debt financing pattern of the companies, there is great fluctuation over the period of time, but the overall trend in debt financing of all the companies is shrinking for the period under study except the Ultratech cement Ltd, which increase the use of debt financing in its capital structure in the study. In case of ACC cement, there is an increasing trend in the equity financing over the period of time at the fluctuating rate as compare to the decreased debt financing. On the other hand, there is large fluctuation in the growing trends of debt financing in the companies of ACC cement, Ambuja cement and Chettiend cement But, in the overall analysis of J.K cement ltd company, in the initial year there is maximum growing trend in the debt financing but after that there is a sudden decrease in the trend in the later period, in the last year the trend again rise which was not as equal to the earlier growth. In case of J.K Cement, In spite of various fluctuations in the debt financing pattern of the company, the debt capital is still increasing at higher rate as compare to the equity capital over the period of time under study. As far as the objective of the study to measure the impact of change in capital structure pattern on the investment of the companies over the period of time, the analysis states that all the companies are increasing their investment level every year at a consistent growth rate along with the increase in the capital structure pattern except the Chettinad cement company, in the earlier year the company invested a constant negligible rate of investment(0.58%) for four years, from 2012-13 the company had a paused the investments. On the other hand, the overall analysis of investment and capital structure pattern of all the companies concluded that growing rate of investment pattern of all the companies is less the growing rate of capital structure over the period of time. Similarly, It can also be said that, most of the pharmaceutical companies are not using their long term sources of funds not only to finance their long term investment, but also to finance their current assets, which states the objective of the companies to get maximum profitability over the period of time along with the long term solvency at less financial risk.

CONCLUSION

In the recent time, financial manager always plans an optimum capital structure for his company to obtain the higher market value per share. An optimal capital structure is usually defined as one that will maximizing shareholder's wealth by minimize the firm's cost of capital. (Trisha, 2015) Capital structure decisions have great impact on the firm's financial performance. Exactly how firms choose the amount of debt and equity in their capital structures still an enigma. There are number of factors influencing the capital structure decision of the company, but the judgment of the person making the capital structure decision plays a crucial part. Two similar companies can have different capital structures as per the different judgment of decision makers with the significance of various factors. Thus, the financing decisions have no effect on firm value, as it is the residue of the more important investment decisions.

his study also conclude that the capital structure decision of the cement companies has very little effect on its investment pattern, which defines that the company is using long term sources of funds to finance its current assets and its operational activities of its business with the object to attain the long term solvency and maximizing profitability with least cost of capital.

BOOK REFERENCES:

1. Gupta, S. K. (2011), *Form of Capital, Financial Management Theory and Practice*, Kalyani Publishers, New Delhi
2. Kishor M. R. (2010), *Financial Management problems and solutions,* Taxmann Publications Pvt Ltd, New Delhi

JOURNAL REFERNCES

1. Bhat, Ramesh, and I. M. Pandey, (1994) Dividend decision: A Study of Managers' Perceptions, Decision, *Saga journals, Journal of emerging market finance,* Vol. *21*, pp. *67–86*.
2. Jackling, B., & Johl, S. (2009). Board structure and firm performance: Evidence from India's top companies. *Corporate Governance: An International Review*, Vol. *17(4)*: pp. *492-509*
3. Md. Abdur Rouf, 2015. Capital Structure and Firm Performance of Listed Non-Financial Companies in Bangladesh. *The International Journal of Applied Economics and Finance*, Vol. *9*: pp. *25-32*
4. Myers, S. C. (1984). The Capital Structure Puzzle, *the Journal of Finance*, Vol-*(3)*, pp. *575-592*.
5. Puwanenthiren Pratheepkanth, (2011), Capital structure and financial performance: evidence from selected business companies Colombo stock exchange Srilanka; *International Refereed Research Journal* Vol.– *II*, Issue –*2*,April 2011
6. Sudesh kumar, Dr. Bimal anjum, Dr.Suman nayyar,(2012), Financing decisions : A study of pharmaceutical companies of India, *International journal of marketing, finance services and management research,* Vol.*1* No. 1, January 2012,
7. Carelton. W.T. and Siberman. I.H. (1977) ―Joint Determination of rate of return and capital structure; an econometric analysis‖; *Journal of Finance*; Vol.*32*; pp.*811-821*.