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Industry Influence on Capital Structure – A Case Study of Five Major Industries of India During 1982-83 to 1991-92.

For more than three decades financial economists have tried to cope with the issue of whether or not there exists an optimal capital structure that will maximize the value of the firm. During the time many models have been proposed to explain observed capital structure, both domestically and internationally, but we know relatively little about why firms finance the way the do.

The problem of companies while raising funds is whether to raise debt or equity capital or both. Though there is continuing theoretical debate on this issue, relatively little empirical evidence exists on how companies actually select between financing instruments. Inspite of the fact that each management makes its own decisions regarding its capital structure, there may be certain general factors which seem to influence the capital structure of an enterprise.

The primary purpose of our study has been to obtain a deep insight into the problem faced by Indian companies in need of funds. An attempt has been made to judge and justify the influences of several institutional characteristics on the corporate capital structure.

We investigate the relationship between debt equity ratio. (dependent variable) and assets composition, business risk, corporate size, debt service capacity, grcwth rate, earning rate, industry class and ownership pattern (independent variables).

The study has been made with reference to sixty selected companies which belong to Automobile, Engineering , Textile, Chemical and Iron & Steel Industries of the

Public and Private Corporate sectors in India. Out of these sixty companies thirty-eight companies from private sector and twenty-two from public sector were selected.

Our first six hypotheses i.e. assets composition effect, business risk effect, corporate size effect, debt service capacity effect, growth rate effect and earning rate effect on the corporate debt-equity ratio-were analised with the help of Multiple Regression and the last two hypotheses i.e. industry class effect and ownership pattern effect were analysed with the help of one way ANOVA (parametric test).

With the help of Multiple Regression, the data were analysed from various angles. In empirical analysis I, inter industry relationship of determinants with capital structure were tested. In empirical analysis 2, we have analysed public sector and private sector companies separately. In empirical analysis 3, intra-industry relationship of determinants with capital structure were tested.

It is clear from the results that some of the selected variables are statistically significant, whereas others are not. In the wake of these results, every company should design its capital structure after considering the influences of these determinants on debt equity ratio.

Hence, the problem faced by companies, while raising funds, can be solved to a great extent, by properly analysing and balancing the above mentioned possible determinants that influence the capital structure.

Debasish Chakrabarti