CHAPTER 7 - EPILOGUE

“To know more is better than to have more”.

The primary objective of this study was to find out the extent of efficacy of the select corporate finance theories. An attempt was made by the researcher to fulfill this objective, by analyzing the Selected, Quality research papers and/or research articles in the light of the normative statements, which were representative statements of the Theory/Approach/Concept.

The select theories were broadly classified in four types viz. financing decisions, investing decisions, dividend decisions and other decisions. The relevant theories/approaches and/or concepts were considered pertaining to the four broad types.

7.1 HYPOTHESIS TESTING

The descriptive statistics of the data yielded overall mean values for all four types as

- The Financing Decisions  -0.00165
- The Investing Decisions  -0.00421
- The Dividend Decisions  0.000348
- Other decisions       -0.00227

It is evident that in all four cases the mean values are near 0. When the value is 0 or near 0 it signifies that, the theory is neither entirely proved nor entirely rejected. When results of this study were being compiled, researcher observed that, results in case of a specific theory/approach/concept were not consistent. When the demography was differing, or when the time
period was differing then, the observations noted by various researchers studying the specific aspect of theory also differed.

7.2 A REFRESHING LOOK AT THE DEVELOPMENT OF THEORIES

The development of any theory takes place in a pattern; this pattern has a chronology viz.

Hypothesis → Concept → Approach → Theory → Facts (based on scientific base). The development of corporate finance theory is no exception to this.

Any research study commences with the Hypothesis, which is an intellectual statement about an event, object or phenomenon. It is a supposition or proposed explanation based on the basis of limited evidence as a starting point for the further investigation.

Concept is a general idea derived or inferred from the specific instances or occurrences, something formed in mind, a thought or a notion. Approach is a way of dealing with a situation or problem. It has been observed that finance is circularly moving from hypothesis to concept and again back to hypothesis. The crystallization of hypothesis into a full-fledged theory has become a rarity.

This is the very reason that, there appears to be a state of confusion leading towards chaos. In the event of theoretical development, the process of demystification takes place and clarity in thought emerges. After thoroughly reviewing the data, researcher finds the lacuna between the theoretical wisdom and real life evidence, with respect to select corporate Finance Theories. The revisit to the corporate finance theory is not leading to definite conclusive inference. No Common thread is found while researcher made an effort to study the select corporate finance theories.

Theory- There is intricate relationship between theory and fact. Theory is confused with speculation, and theory remains speculation until, it is proved.
Facts- are thought to be definite, certain, without question and self-evident. Facts are empirically verifiable observations. Theory and fact are in constant interaction.

*Facts redefine and clarify theory.* Theory is a general expectation, while demographic facts are specific.

### 7.3 GOIND BEYOND HYPOTHESIS

Following findings were noted by the researcher:

Methodologically all the research papers are correct, yet no empirical universalization of any theory is observed.

The Theory is developed on empirical evidence and for empirical evidence, large and reliable data is essential. In Corporate finance function, such large & reliable data is not available. By data we mean Factual information, especially information organized for analysis or used to reason or make decisions.

Historical Vs. Notional Data- Historical data is a past and notional data is a guess, at times not even an intellectual guess.

Journey from conceptualization to theory is not getting momentum. In Corporate finance words are being loosely used for instance, M M Approach / M M Hypothesis , Signaling Theory etc, all these are in reality concepts.

The scientific precision of natural science or aptly developed social science, that precision is not observed in finance.

Finance is circularly moving from hypothesis to concept and back. The present state is, Assumption + Assumption = Confusion.
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7.4 THE NEED FOR CORPORATE FINANCE DATA REPOSITORY

What could be the major reason/s behind such a state of confusion? Researcher assigned following reason/s, the notion of ‘Wealth is personal’ is a deterrent for availability of Data. At personal as well as corporate level the data pertaining to wealth is not available, so notional data is used by almost all the Researchers.

Data which needs to be made open in public domain, as a matter of statutory requirement is revealed. The lack of data is a major limitation for the development of clarity. However, notional data can be rationalized, if the academic fraternity has an access to a large Data Repository. Economics has a large National Level data available hence the Science of Economics became more powerful.

The scenario in the developed countries is shade better. The availability of data for Fortune-500 firms is robust and reliable. However in case large firms the data available are not as robust as the Fortune-500 firms data. The availability of data for Small and Medium Enterprise (SME) sector is even poor.

No common size and / or Comprehensive and / or compatible data is available. Most of the literature available in the domain of the corporate finance theories has been developed in the
context of the data available, that of western world. The specificity of demography is seldom considered while accepting a theory or concept.

Say for instance, Pecking Order theory, which was popularized by Myers and Majluf (1984). This theory proposes that equity financing is less preferred. To be an accepted theory it should be universally acceptable, irrespective of the geographical foundries and the size of the firm. However in reality, this pecking order model was never accepted universally. This model was showing weak acceptance, where the capital markets were underdeveloped.

While analyzing the data, as part of the study, certain peculiar research papers were read by the researcher. The titles of these papers were self explanatory. The Capital Structure Puzzle, Stewart C Myers (1983), The Dividend Puzzle: Review of Dividend Theories, Seppo Kinkki (2001), A Review of New Issue Puzzle, S Ghon Rhee (2002), The Corporate Finance Structure Puzzle, Errol D’ Souza(2002). These papers are some of the representative papers, where the individual researchers have raised peculiar questions about the theory or concept. These questions are not answered by the existing corporate finance theories.

The questions have remained questions. A lot of management thinkers and eminent researchers are studying these pertinent questions; however they are yet to arrive at a logical solution. A lateral view must be adopted to address to these types of questions. An inter-disciplinary approach must be used then a viable solution can be thought of.

Corporate finance as a discipline of study has been evolved from the Science of Economics. In pursuit of the unanswered questions the foundries of finance be crossed and probable answers be searched by having an inter-disciplinary view.

The applicability of the theoretical knowledge should not be confined to the text books only. If a Prudent comparison of Management Science is made with that of Medical or Engineering
Science then it is evident that these sciences rely largely on the theoretical wisdom, and hence the dynamic approach is followed, which in turn gives impetus to the development of the theory. The dictum of Theory Guides and Practice in the field of corporate finance is not fully followed.

Which means when there is diversion of theory and practice? The usefulness of theory is questionable. The academic fraternity needs to revisit the Corporate Finance theories and need to have a critical re-look at these theories. The preaching’s of the theories, not showing any evidence need to be amended. The belief in the theoretical knowledge should be solidly backed by the evidence from the practical life.

7.5 SOME UNRESOLVED ISSUES IN CORPORATE FINANCE

After studying all the research papers critically selected, this researcher strongly feels, a confusion leading to chaos persists in the (select) corporate finance theories.

The demystification is possible if future research is carried out in following areas:

1. The possibility of Information Symmetry
2. The Judicious Proportion of Debt and Equity in the capital Structure of the firm.
3. Possibility of Optimum debt level.
4. Relationship between profitability and firm size.
5. Role of a manager as an agent of the shareholders.
6. The notion of Value Maximization and its effect on firm’s size.
7. Rationale behind paying the dividend.
8. Correlation between extent of profitability of the firm and dividend paid.
9. The extent of cash firm needs to maintain for a rainy day.
10. Post merger decrease in value of the acquiring firm.
11. Reasons behind Tunneling effect followed by Indian business groups.


13. Is Superiority of E V A as a tool of performance measurement, really justified?

This list can be made even exhaustive, however these are some of the representative questions which have grossly remained unanswered.

After reviewing and analyzing the selected Corporate finance theories. This researcher sincerely has got convinced that rather than having plethora of theories, it is in the interest of the society to have a meaningful bunch of theories showing consistent and uniform result.

Researcher would like to conclude by quoting a few lines of a renowned poet, which are aptly relevant to most of the theories of Corporate Finance, where confusion / chaos are persistent.

_I have studied now philosophy_  
_and Jurisprudence, Medicine_  
_and even alas, Theology_  
_from end to end with labor keen;_  
_and here, poor fool, with all my lore_  
_I stand no wiser than before- Faust._

_Johann Wolfgang Von Goethe_