

AN INVESTIGATION IN TO CAPITAL STRUCTURE ISSUE:

A CASE OF NEPAL

Submitted By:

Nagindra Chamlagai

Tribhuvan University campus

Campus Roll No:- 252/2065

T.U. Regd. No:- 7-2-214-359-2005

Exam Roll No:-280298

Submitted To:

Office of the Dean

Faculty of Management

Tribhuvan University

In Partial Fulfillment of the Requirements for the

Master's Degree of Business Studies (M.B.S.)

Kirtipur, Kathmandu

July 2012

RECOMMENDATION

This is to certify that the thesis

Submitted By:

Nagindra Chamlagai

Entitled:

AN INVESTIGATION IN TO CAPITAL STRUCTURE ISSUE

A CASE OF NEPAL.

has been prepared as approved by this Department in the prescribed format of Faculty of Management. This thesis is forwarded for examination.

.....

.....

.....

Prof.Dr.Radheshyampradhan

Prof.Dr. Balkrishna Shrestha

Prof. Dr. Dev Raj Adhakari

Thesis Supervisor

Chairperson of Research

Head

Committee

Central Department of Management

Date:

VIVA-VOCE SHEET

We have conducted the viva-voce examination of thesis

Presented by:

Nagindra Chamlagai

Entitled

AN INVESTIGATION IN TO CAPITAL STRUCTURE ISSUE: A CASE OF NEPAL

And we found the thesis to be the original work of the student written according to the prescribed format. We recommended this thesis to be accepted as partial fulfillment of the requirements for Master's Degree of Business Studies (M.B.S.)

Viva-Voce Committee

Chairperson (Viva-voce Committee) :

Member (Thesis Supervisor) :

Member (External Expert) :

Date:-

DECLARATION

I hereby declare that the work reported in this thesis entitled An Investigation In to Capital Structure Issue: A case of Nepal have submitted to Faculty of Management, Tribhuvan University is my original work. It is done in the form of partial fulfillment for the Master's of Business Studies (M.B.S.) under the supervision and guidance of Prof. Dr. Radheshyam Pradhan.

July, 2012

.....

Nagindra Chamlagai

Researcher

Acknowledgements

This study could not have been completed and produced without the help of many people. It is my great privilege to complete this study under the able guidance of respected Pro. Dr. Radheshyam Pradhan, Faculty of Management, Tribhuvan University, Kirtipur. I wish to express my gratitude to him for his inspiration, regular guidance, generous rapport and support and his unmatched patience that he had bestowed on me in the preparation of this report.

I am very much grateful to the Nepal Stock Exchange Ltd. (NEPSE) and Security Board of Nepal (SEBON), Kathmandu, for their kind co- operation for my research work. It was a great opportunity for me to learn things from them where I could secure valuable experience.

I am also indebted to my respected teachers of University Campus, who have assisted from their respected sectors. I am also thankful to the library members of Central Department of Management and Central library of Tribhuvan University

I would like to express heartfelt thanks towards all the members of my family who provided regular inspiration and contribution for my success.

Thanks

Nagindra Chamlagai

TABLE OF CONTENTS

	Page no.
Recommendation	
Viva Voce Sheet	
Acknowledgment	
Declaration	
Table of Contents	
List of Tables	
Abbreviation	
CHAPTER ONE	
INTRODUCTION	1-11
1.1 General Background	1
1.2 Statement of the Problem	4
1.3 Objective of the Study	10
1.4 Organization of the Study	11
CHAPTER- TWO	
REVIEW OF LITERATURE	13-36
2.1 Conceptual framework	12
2.1.1 The irrelevance proposition	13

2.1.2 Toward and optimal financing policy	15
2.1.3 The trade of theory	16
2.1.4 Capital structure with financial distress and agency costs.	18
2.1.5 Trade-Off theory of Capital structure	19
2.1.6 The pecking order Theory of financing Choices	20
2.1.7 Determinants of capital structure	21
2.2 Review of major related studies	22
2.2.1. Review of Related Studies	22
2.2.2. Review of Nepalese studies	31
2.2.3. Concluding Remark	34

CHAPTER THREE

RESEARCH METHODOLOGY 37-49

3.1. Research Design	37
3.2. Nature and Sources of Data	37
3.3. Selection of firms	39
3.4. Variables and Measures	39
3.5. Data Presentation and Method of analysis:	42

3.6. Development of hypothesis	42
3.7. Financial Analysis Tools:	44
3.8. Statistical Analysis Tools:	45
3.9. Definition of key terms	48
3.10. Limitation of the study	49

CHAPTER FOUR

PRESENTATION AND ANALYSIS OF DATA 51-93

4.1 Presentation and analysis of secondary data	51
4.1.1 Introduction	51
4.1.2 Analysis of Secondary Data	56
4.1.3. Descriptive Statistics Analysis	56
4.1.4. Correlation coefficient	66
4.1.5. Determinants of capital structure in all selected companies.	68
4.1.6 Determinants of capital structure in manufacturing companies.	70
4.1.7 Determinants of capital structure in Non-Manufacturing Companies	72
4.1.8. Concluding Remarks.	75

4.2 Presentation and analysis of Primary data	
4.2.1 General Background	76
4.2.2 Respondents' Profile	77
4.2.2.1 Nature of Sample	77
4.2.2.2 Position and Age	78
4.2.2.3 Number of Employees	79
4.2.3. Analysis of Survey Results	80
4.2.4. Concluding Remarks	91

CHAPTER- FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS 94-101

5.1 Summary	94
5.2 Conclusions	98
5.3 Recommendations	99

BIBLIOGRAPHY

APPENDIX

LIST OF TABLE

Table on.	Title	Page No.
2.1	Empirical studies on capital structure	23
2.2	study on capital structure in Nepal	24
3.1	Firms Selected for the Study	39
3.2	Variables and Their proxies	40
3.3	Testable hypotheses of capital structure determinants	43
4.1	Total debt to total assets ratios for the selected companies	57
4.2	Long term debt to total assets ratios for the selected companies	58
4.3	Short term debt to total assets ratios for the selected companies	59
4.4	Natural logarithm of Sales for the selected companies	60
4.5	Book value of FA to total assets ratios for the selected Companies	61

4.6	Current assets to current liabilities ratios for the selected Companies	62
4.7	Percentage in total assets ratios for the selected Companies	63
4.8	Depreciation to total assets ratios for the selected Companies	64
4.9	Selling and administrative expenses to net sales ratios for the selected companies	65
4.10	Correlation coefficient of all sample companies	67
4.11	Regression results-All sample Companies	69
4.12	Regression results-Manufacturing sample Companies	71
4.13	Regression results-Non-Manufacturing sample Companies	73
4.14	Line of business	78
4.15	Position/ Age of Respondents	79
4.16	Number of Employees in Sample Companies	80
4.17	Systematic Measurement of financial leverage	81
4.18	Measure of financial leverage	83
4.19	Optimal Debt Capital Ratio	84

4.20	Practice of optimal capital structure	85
4.21	Use of debt capital in Nepalese firms	86
4.22	Observation on corporate capital structure policy as viewed by all respondents	87
4.23	Capital structure affects the market price of shares	88
4.24	Purpose of using debt capital	89
4.25	Determinants of capital structure	90

ABBREVIATIONS

Lev ₁	:	Leverage 1 (Ratio of total debt to total assets)
Lev ₂	:	Leverage 2 (Ratio of long term debt to total equity)
Lev ₃	:	Leverage 3 (Ratio of Long term debt to long term debt plus equity)
CVA	:	Collateral value of assets
LQD	:	Liquidity position
NDTS	:	Non debt tax shield
GR	:	Growth Opportunity
FS	:	Firm size
NEPSE	:	Nepal stock exchange
SEBON	:	Security board of Nepal
TU	:	Tribhuvan University
TOT	:	Trade-off- theory
POT	:	Pecking order theory
FS	:	Firm size
ROE	:	Return on equity
PV	:	Present Value