

CHAPTER I

INTRODUCTION

1.1 Background of the Study

The term capital structure is used to represent the proportionate relationship between debt and equity. Equity includes paid up share capital, share premium and reserves and surplus (retained earnings). The market value of the share may be affected by the capital structure decision. The company will have to plan its capital structure initially at the time of its promotion. Subsequent whenever funds have to be raised to finance investments a capital structure decision is involved the process while making the capital structure decision, the dividend policy of the company should be considered. The new financing decision of the company may affect its debt equity mix. The debt-equity mix has implications for the shareholders' earnings and risk, which in turn, will affect the cost of capital and the market value of the firm. Thus, optimal capital structure maximizes shareholders' wealth and minimizes overall cost of capital; therefore it is one of the most important decisions that are taken by financial manager.

The basic objective of capital structure is to determine the proper mixed of debt, preferred stock and equity that will minimized composite coat of capital or maximized the market price of the share. Different sources of financing are used to finance current and fixed assets. The source of financing may be short term and or long term, but they are usually grouped into debt and equity which represents the firm's financial structure. A distinction is usually made between financial structures. Financial structure refers to all sources of finance which both short term and long term that cover the financing of entire assets of a firm whereas

capital structure is the capitalized part of a firm's total financing which includes only the long term sources such as long term debt equity. Thus the capital structure is a part of the financial structure.

Capital Structure = Financial Structure – Current Liabilities

Capital structure concept holds a major place in the financial management. A balance capital structure is the prerequisite for successful business organization and it plays an essential role in acceleration of the economic growth of nations. Obviously, there are various sources of capital, which differ in nature and cost associated with them. The success of any business also largely depends upon the capital structure. Financing the firm's assets is a very crucial problem in every business and as a general rule there should be a proper mix of debt and equity capital in financing the firm assets.

The firm's mix of different securities is known as capital structure. The choice of capital structure is fundamentally a marketing problem. The firm can issue dozens of distinct securities in countless combinations but it attempts to find the particular combination that maximizes its overall market value (Richard: 1991, 397). The practice for optimum capital structure in the united state and European countries are also relevant in developing countries, despite the across these developing countries. (Booth, Varouj, Kunt & Marsimovic 2001:117)

The cost of capital refers to the discount rate that would be used in determining the present value of the estimated future cash proceeds and eventually deciding whether, the projects worth undertaking or not (Barges, 1963:2).

1.2 Statement of the Problem

A firm's basic resource is the stream of cash flows produced by its assets. When the firm is financed entirely by common stock, all those cash flows belong to the stakeholders. When the firm issues both debt and equity securities, it undertakes to split up the cash flows into two streams, a relatively safe stream that goes to the debt holders and a more risky one that goes to the stockholders.

The firm's mix of different securities is known as its capital structure. The firm can issue dozens of distinct securities in countless combinations, but it attempts to find the particular combination that maximizes its overall market value.

Are these attempts worthwhile? Modigliani and Miller (June 1958) showed that financing decisions don't matter in perfect market. Their famous "Proposition I" states that a firm can not change the total value of its securities just by splitting its cash flows into different streams. The firm's value is determined by its real assets, not by the securities it issues. Thus capital structure is irrelevant as long as firm's investment decisions are taken as given.

Toward an optimal financing policy Modigliani-Miller (1958) permanently changed the role of economic analysis in discussion of capital structure; their works provide no explanation for the corporate financing policies observed in practice. The MM irrelevance proposition tells us that if corporate financing policies affect the value of the firm, they must do so by changing the probability distribution of the firm's cash flows. The cash flow distribution can be affected by the choice of financing policy because there are important tax consequences, or because contracting and agency costs are important, or because there are

other important interdependencies between the choice of financing policy and the choice of investment policy.

Modigliani-Miller (1963) argued that since the corporate profits tax allows the deductions of interest payments in calculating taxable income, the more debt in the capital structure, the lower the corporate tax liability, the higher after tax cash flows, and the greater the market value of the firm.

Miller (1977) argued that the tax advantage of debt is exaggerated by considering the corporate profit tax in isolation from personal income taxes. He argued that the corporate tax advantage of debt is offset by personal tax rates on investors' debt income that are higher than tax rates on investors' equity income. In addition, Brennan/Schwartz (1978) also argued that the corporate tax advantage of debt is lower because the interest tax shield is lost if the firm goes through bankruptcy liquidation. DeAngelo/Masulis (1980) argued that substitute tax shield, such as investment tax credits, also reduce the corporate tax advantage of debt.

Kraus/Litzenberger (1973) formalized the argument that the corporate tax shield is offset by increased expected bankruptcy cost, to produce the theory of the optimal capital structure. Increases in leverage increase the probability of bankruptcy and thus increase expected bankruptcy costs. The point at which additional leverage generates an increase in expected bankruptcy costs that just offset the tax subsidy to the incremental debt defines the optimal capital structure.

Jensen/Meckling (1976) used the agency framework to provide a positive analysis of the effects of conflicts of interest among shareholders, managers, and bondholders on the investment and financing decisions of the firm.

After many years of debate, most finance theorists are now in agreement about whether an optimal capital structure exists for a firm, and if so, how it can be determined. The great debate between the so-called traditionalists and the Modigliani and Miller school of thought has apparently ended in a compromise. When taxes and bankruptcy costs are considered, a firm has an optimal capital structure determined by that particular mix of debt and equity that minimizes the firm's cost of capital for a given level of business risk.

This study is mainly concerned with the capital structure management of the manufacturing & processing firms of our country which are listed in Nepal Stock Exchange. Therefore, it would be better first to define the term capital of the manufacturing & processing firms. The term capital consists of equity capital, capital surplus, retained earnings, and treasury stock. Similarly, debt includes loans and bonds/debentures. Capital provides a cushion that protects the firm from insolvency when the value of its assets falls. A firm can meet its obligations to depositors as long as losses on its asset portfolio do not exceed its capital.

For the purpose of this study, variables have been taken to explain the capital structure management of the firm by considering the three principal theoretical models of capital structure; the Static Trade-Off Model (STO), the Pecking-Order Hypothesis (POH), and the Agency Theoretic Framework (ATF). In STO model, capital structure moves towards a target that reflects tax rates, assets type, business risk, profitability and the bankruptcy. In the ATF model, potential conflicts of interest between inside and outside investors determines an optimal capital structure that trades off agency costs against other financing costs. The nature of the firm's assets and growth opportunities are important factors of agency costs. In POH model, financial market imperfections

are central. Transaction costs and asymmetric information links the firm's ability to undertake new investments to its internally generated funds. If the firm must rely on external funds, then it prefers debt to equity due to the lesser impact of information asymmetries as explained by Myers and Mujluf (1984).

1.3 Objectives of the Study

The main objectives of this study are:

-) To examine whether there exists capital structure management practices in the manufacturing and processing companies of our country.
-) To examine the degree of sensitivity of the variables chosen in this study in determining the capital structure of the manufacturing and processing companies. In other words, to examine whether the chosen variables affect the capital structure of the manufacturing and processing companies.
-) To examine the views of the financial officers of the manufacturing and processing companies regarding the capital structure management of manufacturing and processing companies.
-) To examine whether there exists significance difference in capital structure management between the manufacturing and processing companies.
-) To know the relationship between the figures shown on the assets side and the liability side of the balances sheet.
-) Analyzing different financial ratios of there companies and to provide suggestive framework for their improvement.

1.4 Limitation of the Study

This study aims to review of capital structure of selected manufacturing and processing companies of Nepal. But due to the time and scope constraint the study doesn't cover the entire concern of financial management of the companies. The study is not bounded by the fixed standard of measurement and relationship between two or more variables with capital structure. So capital structure relationships with other variables are analyzed on the basis on average.

So the limitations of the study are as follows:

- Only six companies are chosen as sample study out of the 29 listed companies in Nepal Stock Exchange.
- Only last five years data has been used
- Because of strict policy of the company, personal visit to all over the companies and the survey of their system are nearly impossible
- The study totally based on secondary data
- Financial and statistical tools and techniques have been used for analyzing data
- It is prepared for the partial fulfillment of MBS program of TU so it is not a comprehensive study

1.5 Significance of the Study

The explosive growth of investing and raising capital in the global market has put new emphasis on a policy which strives for zero working capital. The worldwide financial analyst, researchers, users, regulatory bodies are involved in great effort in the management of capital structure. Thus the analysis of selected companies' capital structure through this study will lead to shed light on their financial performance. This will give an overview of status of manufacturing companies of Nepal and the

linkage between successful operation and capital structure. In addition, study will helpful for provide a glimpse of manufacturing companies in Nepal and their historical trend.

1.6 Methodology of the Study

Population and Sample Size

There are 29 manufacturing and processing companies listed in Nepal Stock-Exchange at the end of year 2005. Due to some constraints it is not possible to consider all these companies for the purpose of this study. At least 9 companies should be considered for both population and sample for this study.

Nature and Source of Data

This study, basically, depends upon the secondary data and which will be collected from the published financial statement of selected manufacturing and processing company. In addition, necessary information will be collected from the concerned firm. However, to some extent primary data will also be collected through questionnaire to different financial officers of various firms to acquire their views regarding capital structure of the manufacturing and processing company. In case of need, personal interview with the key persons of the firm and persons concerning with the firm will also be considered. The data will be collected for the purpose of study from 1991 onwards.

Method of Analysis

For the purpose of this study, variables have been taken to explain the capital structure management of the manufacturing and processing company by considering the three principal theoretical models of capital structure; the **Static Trade-Off Model (STO)**, the **Pecking-Order**

Hypothesis (POH), and the Agency Theoretic Framework (ATF). The following are the variables taken for the purpose of the study.

Dependent Variables:

-) Debt Ratio = Total Liabilities / Total Assets
-) Long Term Debt Ratio = Long Term Debt / (Long Term Debt + Net Worth)

Independent Variables:

-) Tax Rate
-) Business Risk
-) Assets Tangibility
-) Size (In terms of revenue generated)
-) Return on Assets

Based on the data and variables, the Multiple Regression Equation model will be used to determine the degree of sensitivity of each independent variable. The model can be expressed as:

$$D/V = \alpha + \beta_1 X_1 + \dots + e \text{ and}$$

$$P_s = \alpha + \beta_1 X_1 + \dots + e$$

Where,

P_s = Market Price of Share

D/V = Debt Ratio and Long term Debt Ratio

α = Intercept of equation

β_i = Coefficient of the i th explanatory variables

X_i = the i th explanatory variables

e = random error term

1.7 Organization of the Study

Chapter one will consist introduction, statement of problem, objective of the study, and limitation of the study, need for analysis.

Chapter Two relates to Research Methodology and includes nature and sources of data, data collection procedures, data presentation and analysis and.

Chapter Three is the final chapter of the study. This is the summary of the whole study. The conclusion of the study will be presented in this part.

Chapter Four contains presentation and analysis of data. In this chapter data are derived through balance sheet and profit and loss account and presented in tables then analysis and interpretation.

Chapter Five contains summary and conclusion of the study. After that all necessary recommendations are presented.

CHAPTER II

REVIEW OF LITERATURE

2.1 Introduction

This chapter is about review of the literature; also this chapter deals with the review of the capital structure. The more details descriptive manner, for this study of various Books journal and the articles as well as past thesis also review. This chapter tries to detail the conceptual theoretical concept regarding the definition of capital structure theories of capital structure factors of the capital structure. In the context of Nepalese Organization, some of the literature review to these studies are presented below:

2.2 Meaning and Concept

Capital structure plays vital role to increase the probability to insure the maximum return to the equity holders and minimum cost of the capital. First of all we most know that what the capital structure is. In general capital structure is the combinations of the long-term sources for funds such as debt, equity, preference share etc. 'Capital represents the funds available to the company for its business. The capital structure refers to the proportions of findings derive from debt equity. Capital structure is usually measured by the debt equity ratio or by share holders' ratio (McGrath, 1949:171).

'The term capital structure means like proportion of the different type of the securities issued by firm the optimal capital structure is the set of proportion maximized the total value of the firm' (Schells and Helly, 1983:330). Capital structure is the composition of debt and equity that comprises a firms financing of its assets.

Both debt and equity are used in large organization. 'The choice of the amount of debt and equity is made after a comparison of certain characteristics of each kind of the security of internal factors that can external factors that affects the firms. So the capital structure is that permanent financing of the represented primarily by the long-term debt, prefer stock and common equating the rate of return and the cost of capital, capital structure is sought by using a proportion of debt such that the correct degree of trading on equity leading to financial leverage will cause the highest market value of the ordinary shares (Kuchhal, 1977:388). 'Capital structure is made up of debt and equity securities which comprise a firm's finance of its assets. It is the permanent financing of the firm represented by long-term debt plus preferred stock plus net worth (Kulkarni, 1983:363).

Determining a firm's financial structure means to basic question first how should the firm's total sources of fund be divided among long term and short term financing. Second what proportion of firms should be financed by debt and equity is made after the comparisons of the certain characteristics of each kind of internal factors related to the firms operation and of external factors that can affect the firms.

Once the financial manager is able to determine the best combination of debt and equity he or she must raise the appropriate amount through best available source. A capital structure with a reasonable proportion of debt and equity capital is called optimal capital structure with a reasonable structure indicator of the optimum capital structure are net profit earning per share and value a firm.

'As the proportion of debt in the capital structure increase both the cost of equity and cost of debt deign to raise reflecting the increase financial risk but the two do not necessarily raise in the same proportion. Thus with

increasing use of debt the overall cost of capital is to fall because the after tax cost of debt is typically cheaper than the cost of equity. After a while the financial markets considers to science for excessive use debt and to much financial risk, completely offsets the advantage of using the lower cost of debt. So they agree with the statement that the judicious mix of long term debt and equity resulting in higher in a higher profiles and stock prices' (Steven E Bolton Report,).

2.3 Optimal Capital Structure

The optimal capital structure is that capital structure or combination of debt and equity that leads to the maximum value of the firm. Optimum capital structure maximizes the value of the company or shareholders wealth and minimizes the company's cost of capitals. The value will be maximized or the cost will minimum when the marginal cost of each source of the funds is the same. An optimum capital structure would be obtained at those combinations of debt and equity that maximizes that total value of the firm or minimizes the weighted average cost of capital. Optimal Capital Structure can be properly defined as that combination of debt and equity that attains the stated managerial goals maximization of the firms' market value and which maximizes the firm's cost of capital. As the existence of an optimal capital structure

Implies the simultaneous optimization of both the cost of capital and firm's market value occupies central position in the theory of financial management. (Phillipparos, 1947:237). The normative objective of the firm of maximizing stockholders wealth is time in the least "expensive ways" (Kreps and watch, 1975:411).

The Optimal Capital Structure may be defined as the relationship of debt and equity securities. This maximizes the value of firm's equity stock.

It may exit under three situations:

1. The total value of the firm is maximizations when its equity stock is at maximum value market if debt and preferred stock are not affected by fluctuation is market values. The values of equity, stock however fluctuates with profits of a firm.
2. The equity stock value should be maximized on a per share basis so as to ensure to optimal capital structure. The issue of additional share may increase the total value of equity stock but this action may result in a decline in per share value of equity stock and the firms may move away from its optimum capital structure.
3. The optimum capital structure occurs when a firm's overall cost of capital is a lowest point.

The optimal capital structure should be balance between risks and return born by equity shareholders.

Objectives of optimal capital structure are as follows:

-) To maximum return on equity capital
-) To maintain control power
-) To minimize risk
-) To increase flexibility
-) To employ high grade securities

2.4 Factors Affecting Capital Structure

Capital structure of different types of firms must consider the many factors managing directories or major shareholders are major determining factors. After overview of the capital stricture of many organizations.

1. Market conditions:- Conditions in the stock and bond markets undergo both long and short term changes. That can have an important an firm's optimal capital structure for e.g., during the

credit crunch in the winter of 1982, there was simply no market at any reasonable interest rate for new long-term bonds rated, low rated combines that needed capital mere forced to go to the stock market of the short-term debt. Action such as this could represent permanent changes in target capital structure of temporary departures from stable targets. The important the type of securities used for a given financing.

2. Stability of sales and growth rate: - Firms which sales a relatively stable can use more debt and incur higher fixed charges than a company with unstable sales. As far as growth rate is concerned other things remaining the same faster growing firms tend to use somewhat more debt than slower growing companies.
3. Cost of capital: - The optimal capital structure should be less costly. Therefore company use the sources having lower cost. Component cost of capital is comprises of using costs and issuing cost. Hence issuing cost of various kinds of securities should also be considered while raising funds. The cost of floating a debt is generally less than the cost of floating equity and hence it may persuade the management to rise debt financing;
4. Firm's internal condition:- The internal condition of a company also plays an important role on capital structure. According to Brigham's suppose a firm's has just successfully completed an R & D program and project are not yet anticipated by investors and hence are not reflected in the price of the stock. This company will not materialize and reflected in the stock price at which time it might want to sell an issue of common stock retire the debt and return to its target capital structure.

5. Taxes:- Interest is deductible expense while dividends are not deductible hence. The higher a firm's corporate tax rate, the greater, advantage is the advantage is using debt.
6. Profitability:- The firm's health high rates of return of investment use relatively little debt. Their high rate of return enabled them to do most of their financing with retained earnings.
7. Interest rates: - A certain point of time when the general level of interest rates is low, the use of debt financing might be more attractive. When interest rate is high, the sales of stock may become more appealing.
8. Control:- The effects of debt versus stock on a management's control position can influence capital structure. If management has voting control over the company and is not in a position to buy more stock, debt may be a choice debt for new financing. On the other hand, management group that is not concerned about voting control many decide to use equity rather than debt. An excessive amount of debt can also cause bankruptcy which in turn mean a loss of control.
9. Operating leverage:- Other things remains the same a firm with less operating leverage is better able to employ financial leverage. Interaction of operating and financial leverage determines the overall effect of a change in sales on operating income and net cash flow.
10. Flexibility:- Capital structure of a firm should be flexible. Then it affects the future financing decision of the company. Therefore the company should compare the benefits and cost of attaining the desired degree of flexibility and balance them properly.

- 11.Assets structure:- Firms whose assets are suitable as securities for loans tend to use debt rather than having. General purpose assets, which can be used by many businesses make a good collateral, whereas special purpose assets do not thus real estate companies are usually highly leveraged whereas companies involved in technological research employ less debt.
- 12.Legal requirements:- The government has also issued certain guidelines for the issue of shares and debentures. The legal restriction is very significant as these lay down a framework within which capital structure decision has to be made.
- 13.Nature of industry and capital requirement:-The pattern of capital structure of the industry on which the firm is a part is also a very important factor affecting the determination of the capital structure of the firm. The needs and financial condition of a company have to be considered. If growth is only moderate a reinvestment of earnings will serve the purpose.

2.5 Assumption of Capital Structure

The theories of capital structure make certain assumptions, which are given below:-

1. There are two sources of funds used by a firm Debt and equity.
2. There are no corporate taxes.
3. The dividend payout ratio is 100 percent. There is no return earning;
4. The firm life is perpetual;
5. The operation profit is not expected to grow.
6. All the investors have the same subjective probability distribution of the future expected EBIT for a given firm.

7. The total finance is fixed. The firm can change its degree of operating leverage either by seeing share and the proceeds to retire departure or by raising more debt and reduce the equity capital.
8. The business risk is assumed to be constant and independent of capital structure and financial risk.

In the theoretical analysis of capital structure, the following basic symbols have been used.

Cost of debt $k_d = I/B$

Cost of equity = $EBIT - I/S$ or $NOI - I/S$

Overall cost of capital

$$K_o = NOI/V \quad \text{or, } K_o = k_d (B/V) + K_e (s/v)$$

Value of the firm

$$V = B + S$$

Where:

B= Total market value of debt

S= Total market value of stock

V=Total market value of firm (B+S)

K_e = Equity capitalization rate

K_o =Overall capitalization rate

I= Total amount of annual interest

EBIT= Earning before interest and tax

2.6 Theories of Capital Structure

The main question facing financial theorist and corporate managers is the relationship between firm's capital structure and its cost of capital and value. The major Theories are as follows:

1. Net Income (NI) approach
2. Net operating income (NOI)

3. Traditional approach
4. Modigliani-miller (mm) theory
 - a) with taxes
 - b) without taxes

2. 6.1 Net Income Approach

According to the net income approach by the Durand the capital structure decisions relevant to the valuation of the firm. In other word, a change in the financial leverage will lead to the corresponding change in overall cost of capital as well as the total value of the firm. The degree of financial leverage as measured by the ratio of debt to equity is increased. The weighted average cost of capital will decline.

“The emphasis is EBIT is to measure how the degree of leverage brings change in valuation of the firm. Assuming a constant equity capitalization rate the increase in chapter debt funds lowers the weighted average cost of the capital and there by raising the value of the firms and the increasing in debt may not be increasing risky”(Shrestha 1981:28).

The NI approach to valuation is based on three assumptions, which are as follows:

-) There are no taxes
-) Cost of debt is less than of equity
-) The use of debt not change the risk perception of investors as a result cost of equity and cost of debt remains constant with charge in leverage.

The financial leverage is an important variable to the capital structure of a firm. A change in capital structure will lead to corresponding change in overall cost of capital as well as the total value of the firm.

As the proportion of cheaper debt funds in the capital structure increase the weighted average cost of capital decreased and approaches the cost of debt. Therefore firm increased its leverage by increasing its level of debt relative to equity. The overall cost of capital is that it increases the value of the firm.

Overall cost of capital can be expressed by following formula:

$$\text{Overall cost of capital (K}_o\text{)} = \frac{\text{Net operating income}}{\text{Total value of the firm}} \\ = \text{EBIT}/V$$

As per assumption : cost of equity and cost of debt are constant and K_d is less than K_e .

Therefore K_o will decrease.

NI Approach

Where K_e = cost of equity

K_d = cost of debt

2.6.2 Net Operating Income Approach

In this approach, net operating income is capitalized at an overall capitalization rate to obtain the total market value of the firm. As EBIT and overall capitalization rate remain constant capital structure does not affect the market value of the firm market value of the equity is computed after deducing market value of debt firm total market value of debt from total market value of the firm. This theory assumes that the cost of debt and overall cost of capital remains constant with the firm's financial leverage. The required return an equity increase linearly with financial leverage.

Assumption of Approach:

-) The market uses an overall capitalization rate K_o to capitalize the net operating income K_o to depend upon the business risk. If the business risk is assumed to remain unchanged K_e is constant.
-) Debt capitalization rate, k_d remain constant
-) The market capitalization the value of the firm as a whole. Thus, the split between debt and equity is not imported.
-) The use of less costly debt funds increase the equity
-) Capitalization rate to increase. Thus the advantage debt is offset exactly by the increase in the equity capitalization rate K_e .

2.6.3 Traditional Approach

The traditional capital structure theories are taken as middle position. It is a compromise between the NIA and NOIA. The traditional approach to valuation and leverage assumes that there is an optimal capital structure and that the firm can increase the total value of the firm can increase the total value of the firm through the judicious use of leverage. The manner in which the overall cost of capital recast to the change in capital structure can be divided in to under three stages.

1. First Stage:- in this stage with the judicious mix of debt and equity, minimizing the cost of the capital can increase the value of the firm there. During this stage, with the using of debt, the cost of debt (k_d) remains constant due to which the investors penalize the form by raising the cost equity (k_e). However, the cost of capital (K_o) decreased because of the cheaper cost of debt.

2. Second Stage:- After reaching a certain degree of leverage the value of the firm will maximum with the cost of capital minimum.
3. Third Stage:- Beyond a certain degree of leverage on a specific point if the amount of debt is increase also cost of capital their by decreasing the value of the firm.

2.6.4 Modigliani-Miller Approach

The Modigliani-Miller theory relating to the relationship between the capital structure cost of capital and valuation is to the NOI approach. The MM proposition supports the NOI approach relating to the independence of the cost of capital of the degree of leverage at any level of debt equity ratio. The significance of their hypothesis lies in the fact that it provides behavioral justification for constant overall cost of capital and therefore total value of the firm. In other words, the MM approach maintains that the weighted cost of capital does not change in the proportion of debt to equity in the capital structure.

Basic proportion are firstly the overall cost of capital (K_0) and the value of the firm (V) are independent if its capital structure. The second proportion of the MM approach is that cost of equity is equal to the capitalization rate of a pure equity stream plus a premium for financial risk equal to the difference between the pure equity capitalization rate (K_e) and K times the ratio of debt to equity. The third proportion of the MM approach is the cut off rate of investment proposes in completely independent of the way in which an investment is financed.

The proportion that the weighed average cost of capital is constant irrespective of the type of capital structure is based on the following assumption.

- 1) Perfect capital market:- the perfect market means that, security is divisible, there is no transaction cost, investors are free to buy\shell security, investors are rational and behave regionally.
- 2) The dividend payout is 100 percent.
- 3) There is no tax, in this assumption is removed later.
- 4) The risk of investor is defined in terms of the variability of the net operating income, Firm can be grouped in to homogenous risk class. The firms will be considered to belong to homogenous risk expected earning have identical risk characteristics.

MM theory in 1958 proposed that the theory without tax and later with taxes.

MM theory (without tax)

This theory can be expressed in terms of the proportion II and I.

Proportion I

This proportion states that the market value of a firm is independent of its capital structure. MM Average that for firms in the same risk classes, the total market value is independent of debt equity mix and is given by capitalizing the net operating income (NOI) by the rate, appropriate to that risk classes. Which is expressed follows:

$$V = \text{NOI} / K_o \quad \text{or} \quad \text{EBIT} / K_o$$

For Levered firm

$$V_L = \text{NOI} / k_o^L$$

For undelivered firm

$$V_U = \text{NOI} / K_o^U = \text{EBIT} / K_e^U$$

Where

K_e^U = the equity capitalization rate of an undelivered firm

K_e^L = the equity capitalization rate of an delivered firm

V= value of firm

KoV = The overall capitalization rate of an unlevered firm

Ko= Overall cost of capital

KoV= The overall capitalization rate of an unlevered firm

KoL= the overall capitalization rate of a levered firm

VuL= Value of Unlevered firm

VL= Value of levered firm

Proportion II

This theory states that the cost of equity rises proportionally with the increase in the leverage in order to compensate in the form premium for bearing additional risk arising from the increase in leverage. It is that only the equity holders adjust the capitalization rate for the degree of financial leverage risk. It means that K_e increases as debt-equity ratio increases. The K_d doesn't respond to change in debt-equity ratio and it remains constant.

The cost of equity capital for a levered firm (K_{eL}) is equal to the cost of equity of an unlevered firm (K_{eU}) plus a risk premium equal to the difference between K_{eU} and K_u multiplied by the debt-equity ratio.

$$K_{eL} = K_{eU} + K_d \frac{B}{S}$$

Since, $K_{eU} = K_u$, so

$$K_{eL} = K_u + (K_u - K_d) \frac{B}{S}$$

This proportion shows the impact of financial leverage on the cost of equity. Due to the increase in leverage, the firm gets the benefit of cheaper debt, but the benefit is exactly offset by an increase in the cost of equity in the form of risk premium expected by shareholders, against an increase in financial risk.

MM Theory (with taxes)

Under MM theory, the value of a firm is independent of its debt policy is based on the critical assumption that the corporate income tax does not exist. But in reality, the corporate tax exists." In their 1963 article, MM shows that the value of the firm increases with debt due to the deductibility of interest charges for tax computational and the value of the levered firm will be higher than of the unlevered firm "(Panday,1999:694). Thus, the value of a levered firm is equal to the value of unlevered firm plus the present value of interest tax-shield as shown below.

Value of a levered firm = Value of an unlevered firm + PV of interest tax shield

The value of unlevered firm when corporate tax does not exist is,

$$V_u = \text{NOI}(1-T)/K_U = \text{NOI}/K_U$$

The above equation implies that, when corporate tax exists, the value of levered firm will increase continuously with debt. Thus, theoretically value of the firm will be maximum, when it employs 100 percent debt. Because of the tax deductibility of interest charges, a firm can increase its value or lower overall cost of capital by using chapter debt funds. Thus, the optimal capital structure is attained when it employs 100% debt, nor are the lenders ready to lend beyond the certain limit.

Why do companies not employ external level of debt or are lenders not ready to lend beyond the certain limit? Why do companies not employ external level of debt in practice? The reason behind it is that, the borrowing may involve extra costs (in addition to fixed interest cost) like cost of financial distress, which may offset the advantage of using debt. Another reason may be the personal taxes involved for lenders.

2.7 Ratio Analysis Capital Structure

The important ratio pertaining to capital structure may be studied which is given below

1. Debt to total capital ratio: This ratio is proportion of between long term debt and permanent capital. This ratio is proportional of between long term debt and permanent capital. This ratio is variation of debt equity ratio and gives similar indication as the debt equity ratio. An arbitrary rule is that long term debt should not be more than 67 % of the permanent capital.

Debt to capital ratio= Long term debt/Permanent capital

Permanent capital includes all funds provided by outsider an internal source that will remain in the concern for a long period. Long-term debt includes only funds which are provided for long period by outsider.

2. Debt to equity ratio: this ratio is measured of the relative amount provided lender and owners also know it as external-internal equity ratio.

Debt to equity ratio= External equity / internal equity OR Amount of debt/Amount of equity

An average debt to equity ratio up 1:1 is acceptable. The outsider funds include all debts long term loans and debentures. The ownership consist performance share, equity shares, capital reserves retain earning and reserves representing.

3. Debt ratio: the debt ratio is defined as total debt divided by total assets.

Debt Ratio= Total debt/Total assets

This ratio is acceptable for 1:2

4. Net worth to total assets: The ratio of net worth to total assets also called proprietary ratio. It is the ratio of funds belonging to shareholders to the total assets of the company . Funds

belonging to shareholders include share capital plus reserves and surplus. It is the sum of net worth divided by assets, i.e.

Net worth to total Assets Ratio= Net Worth/ Total Assets

It forces attention on the percentage of assets supplied by shareholders. A relatively high proprietary ratio reflects less likelihood of financial difficulty resulting from fixed interest charges and liability to meet maturing debt obligation. A low proprietary ratio indicates a more speculative situation because of the possibility of high profits or losses. Analysts are of the opinion that normally the proportion of net worth to total assets should be 20% to 40 %.

5. Interest Coverage Ratio

It is also known as 'Time interest Earned Ratio'. The ratio measures the debt servicing capacity of a firm in so far as fixed interest on long is concerned.

The interest coverage ratio is the sum of net profit before interest and tax divided by interest charge.

Interest Coverage Ratio=Net profit before Interest and tax / Interest charge

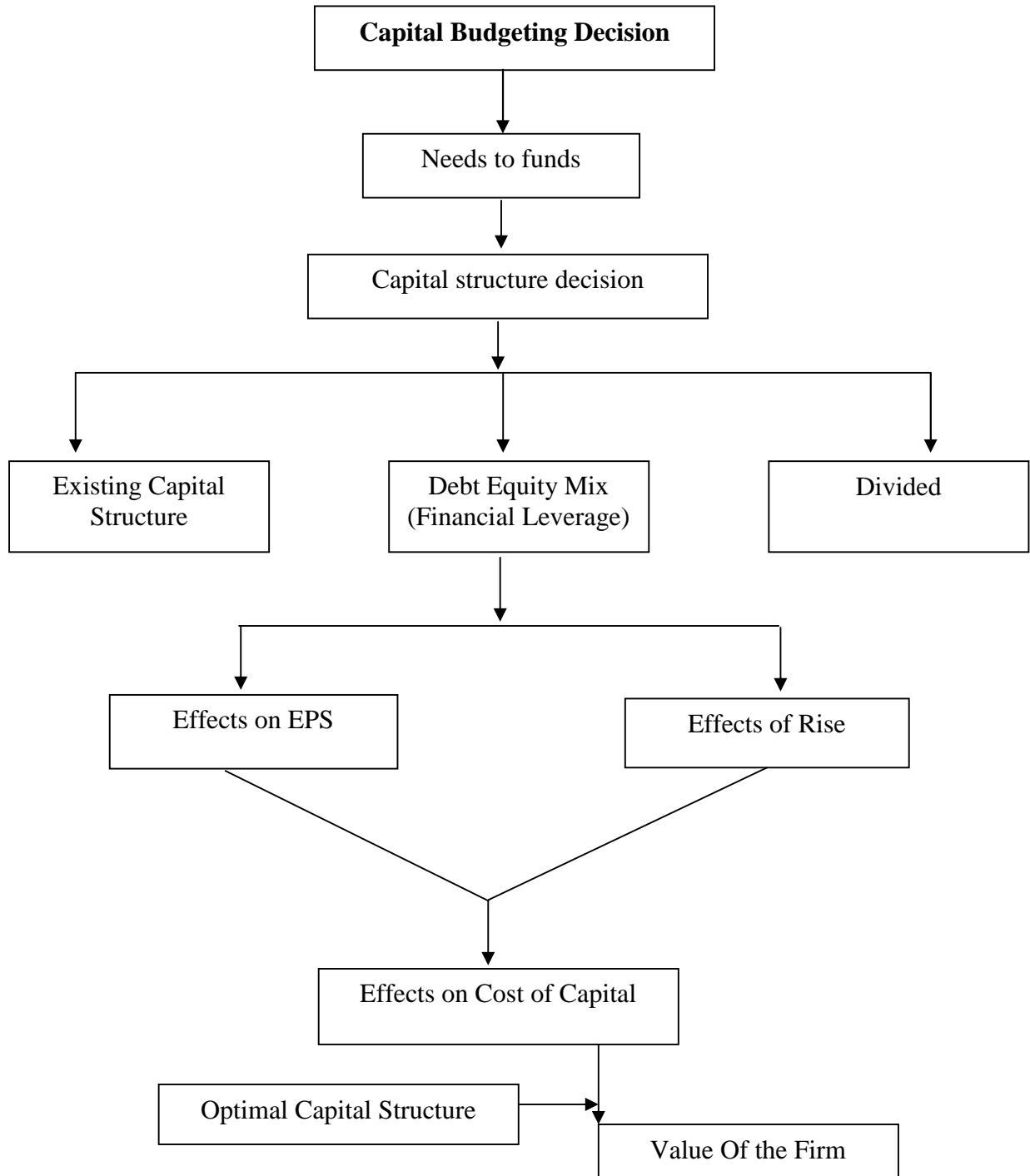
This ratio shows how much time the interest charges are obtained by funds are ordinary available to pay the interest charge. A higher ratio is desirable, but a higher ratio indicates that the firm is very conservative in using debts. A lower ratio indicates inefficient operation.

This ratio shows that demand for funds necessitates a new capital structure decision.

Since a decision has to be made as to the quality and forms of financing this decision had to be made as to the quality and forms of financing this decision will involve an analysis of the existing capital structure and the factors which rule the decision at present the dividend decision also affects debt-equity mix.

The debt equity mix has implication for the shareholders earning and risk, which in turn affect the cost of capital and market value of the firm.

2.8 The Capital Structure Discussion



(Source I M Pandey on eit, P 204)

2.9 Review of Related Thesis

Ramesh R. Arayal conclude on his research titled “An evaluation of Capital structure of Bottlers Nepal Ltd”(1991). He has founded that the long-term debt of BNL is increasing year by year because the company has borrowed more long-term debt.

Ration analysis showed the inefficient capital structure management of the company He had made his analysis only for the five year period and he suggested that the company has to follow good policy to set the capital structure.

The calculation of leverage position indicates the bad performance of the company because it is in increasing trend. After doing all calculation such as ratio, leverage, capital structure position, correlation and P/E etc. He pointed that the company has to lower down the amount of debt and to obtain additional fund through the issue of equity share by using chapter source of collecting fund. In order to build up public image, share must be issued to the general public. More over the company should think about the other new products for winter to increase good image of the company.

Once of the important elements for the present situation is known as insurance. Now a day, people want security for their money and security can be provide for every person with the help of insurance policy, for this purpose, Rastriya Beema Sanasthan has played a vital role in mobilizing in various sectors of the country . Bal Krishna G. C. has mentioned this in his study: “A study on Capital and Assets Structure of Rastriya Beema Sanasthan”(1998). The sound financial position as well as the strength of the company depends to a large existence, on the capital and assets structures. The capital structure of RBS is subscribed as the composition of capital, reserve and fund and balance of amount, current

liabilities Investment cash, and Bank other assets, Total income and expenditure. He has used statically tool such as ratio, percentage, average co-efficient of correlation, standard deviation, Coefficient determination etc. to analyze the component of capital and assets. From his analysis, it is known as capital had been in increasing trend during eight year and all the other components also have been were increasing. During FY 2056/057, the return on assets is changing on percentage basis with negative sign. The overall observation shows that the return on assets in not in favor, so he has suggested that the total assets have to be properly utilization so that net income would increase.

Because of being a mountainous country, Nepal is very difficulty to travel. Most of the places are still unknown to many people due to the lack of road and transportation facilities. Although air transportation is the best way to relief from this problem, there are only few industries, which are able to provide air transportation facilities. Among these all, Necon Air Ltd. is one of the most reputed airline industries in Nepal. It is able to earn enough profit. According to Kamal Bhadur Rajlawat's he thesis entitled, "capital structure of Necon Air ltd."(1999). In his study, he has found that Necon air ltd. has equity ratio higher than its necessity. This higher debt capital structure is serious implication form the firm's point of view. In the condition, the capital structure will lead to inflexibility in the operation of the firm as creditors would exercise pressure and interfaces with management. Necon air has taken debt from different commercial bank as well as owner and has to pay heavy portion of profit as interest. According to the annual report, it has close relationship with Nepal Arab bank ltd. in borrowing loan in different ways but higher portion of the long-term debt has been borrowed form clauer aviation U.K. so the payment of interest will be hazardous when

profit is declining. So Rajlawat suggests that Necon Air Ltd. should decrease its debt capital drastically as far as it can be practicable. He has added that the ratio of 2:1 is the best ratio for optimal structure. That is why the company should reduce its heavy burden of interest payment; the interface of creditors with management and also search for a cheaper source of funds for investment.

Shanti Raj Prasain has done a study on “capital structure of Nepal Bank Ltd.”, (1999).

The basic objective of the study is to analyse the interrelationship and trend among some of the component parts of capital and assets structure. To analyze facts in this study, he has used some of the static tools, such as ratio percentage, index, average and coefficient of correlation. From the study it is known that the bank is composed of its capitals with the major portion of deposit. The total assets of the bank are the composition of loan and advance are the major portion. During the study, total assets and capitals are in increasing trend. But increasing rate of component is different. So the interrelationship of the component is fluctuating. The average growth rate of net profit, and higher than the growth rate of the total expense. The total income and total expenses are not under control to the bank, and the net profit is only 40.64% of the total income. He has recommended that the bank should control total income as well as expenditure and suggested that total deposit and the bank must also control investment. The bank needs to reduce its expansion and control fluctuation in the earnings per share to improve its market price per share.

Kamal Raj Pathak has carried out a study on “On Capital Structure & Profitability: a comparative case study between Nepal Indosuez Bank Ltd. and Nepal Grindlays Bank” (1999). The capital structure of both banks is highly levered, so it is difficult for them to pay interest and

principal that may ultimately lead them to liquidity or bankruptcy. There is no significant relationship between debt and equity ratio in terms of fixed deposits to net worth and overall capitalization rates of the banks. The ROE fluctuation was influenced by the dividend payout ratio and interest margin in NIB Ltd. Both banks vary in the case of total assets, number of bank branches and volume of transactions. Both the bank is efficient and well established and doing well. He has suggested that NIB Ltd. should expand assets and branches, which may ultimately affect the bank's performance and increase the profitability more than ever. It is already stated that Nepal is becoming a center of attraction as a tourism destination. Although in recent days it has been violated by so many reasons, hotel sector, a small part of tourism, is playing a great role in the development of the country. To know about the role of the hotel sector, in the regard, G.B, Tamang, has done a comparative study about two hotels Yak & Yeti and Soltee, a comparative study with the analysis, which is entitled "An Impact of Capital Structure on Profitability" (2001). He found that profit is one of the measurements of successful organization planning its most optimum capital structure to provide maximum return to its shareholders and to increase the value of the firm. By analyzing the debt to equity ratio in terms of long-term debt and shareholders equity, both hotels D/E ratios are not higher according to the standard ratio, which constitute 1:1. Hotel Yak & Yeti is trying to be a levered company, which has practice of increasing the D/E ratio, since 2055/056 by approximately 27% every year. While calculating the correlation coefficient, he found that hotel Soltee has a negative correlation coefficient and there is safety to lenders last year, which is indicated by decreasing D/E ratio. Hotel Soltee does not have financial leverage that is why changes in EBIT are not able to bring change in EPS. Therefore he has suggested that hotel Y & Y should reduce its equity multiplier and

increase the use of assets efficiently, in order to get higher ROE. Both hotels have once higher profit margins but it is impossible to get high profit margin every time. So they should try to increase assets turnover and redeem the amount of total debt, otherwise such debt would be a burden interims of paying fixed interest while hotels are not getting high profits. He has also recommended that they should give equal importance to other factors like operating efficiency and assets affiance, etc and the government also should make effective policy.

Shambhu Prashad Parajuli has studied “Capital Structure and its impact of Profitability of Nepal Liver Ltd.”(2001). He has analyzed that the appropriate mix of capital keeps a firm sound and healthy. In the long run, liquidity may depend on the profitability of firm but to service to achieve long profitability, it has to depend on its capital structure to some extent. He has used hypothesis to measure the significant relationship between debt and equity. Thus it can be said that the company’s management is reluctant towards employing long-term loans. From the DU point analyses. It is found the profit margin and equity multiplier are in decreasing trend, which causes continuous decreases in ROE up. According to different calculation, he has found that performance of NLL is not in satisfactory level. He has recommended the maintenance of proper capital structure by including the long-term debt.

From the review of the above studies on the capital structure and leverage position, it is clear that different persons have presented different result about capital structure and its impact on profitability. Therefore, Ramesh R. Aryal choose BNL for his study and limited his analysis to five years since 1984/85. In the stud, he recommended that BNL should lower down the amount of debt through the issue of equity share. But the present situation of BNL shows the zero amounts in its capital structure.

In the similar study of capital structure and assets and capital structure on profitability of the firm.

A study of financial ratio as Indicators of Profitability “Bhanu Nath Dahal makes a comparison between the banks of Nepal and other country. Bal Krishna finds in his study of capital structure and assets structure of “Capital structure Rastriya Beema Sasthan” that the financial activities mostly depend upon capital and assets structure of the company.

Shanti Raj Prashain in his study on “Capital Structure of NB Ltd” analyzed the relationship between different factors of capital and assets. He suggests controlling the expenses for improving market price per share. But MPS is not depending only expense of the firm. The analysis of “Capital structure of Necon Air Ltd” cover the analysis of capital structure of the company only five year. Among 115 listed companies he selected only once company NAL for study work most reputed airlines industry is Nepal.

Sambhu Nath Parajuli’s on “capital Structure Management of NLL” gives the DE ratio of the company however her mentions the low debt level of NLL. In this summary and suggests including long term debt to gain more profit. He focused his study on the short –term debt to gain more profit.

G.B. Tamang has taken only two hotels Soltee and Y & Y for his study. The study is limited to the impact of capital structure on profitability. He recommended that the government should make sound policy towards tourism but without increasing hotel’s capacity and making good plan to attract the tourism, the government alone cannot do.

All the above studies are concerned with the research title “Capital Structure”. Some researchers have selected various companies for the

research and some have concerned in only one institution, But this study includes only manufacturing industries to cover the analytical part and fulfill the objectives of the study. Possibly this study may be the first kind in the area as the study is concentrated in only three manufacturing companies of Nepal listed in NEPSE. It has also analyzed the Du- Point system of analysis.

CHAPTER III

RESEARCH METHODOLOGY

3.1 Introduction

Research Methodology is the way to solve systematically about the research problem.

This chapter incorporates research design. Nature and source of data is population and sample, Data Collection procedure and lastly, method of analysis. This chapter offers the method of investigation followed by the objective of the case study also states the source and limitation of the data use in the study.

3.2 Research Design

A research design is simply the plan structure and strategy of investigation conceived so as to obtain answer to research question and to control variance.(Wolf Pant, 1999:50)

The main objective of this study to analyze the relationship between debt and equity of listed company and provide recommended on the basis of finding to fulfill this purpose. This study follows the analytical and descriptive research design. In other to achieve the objective of the study, secondary data have been used also survey method are used

3.3 Nature and Source of Data

The data used in this study in this study are basically secondary. The secondary data have been collected from financial statement. Annual report from “Nepalsstock.com” the official website of Nepal Stock Exchange Limited. All the collected data and information have been properly synthesized, arranged and calculated to reach at the realistic and analytical synthesized.

3.4 Population and Samples

All listed company in NEPSE is considering as total population. Sample drawn from target population random sampling there are 38 manufacturing companies listed in NEPSE. Out of them, three manufacturing companies have been chosen the basis of multination groupies and public enterprises. The samples manufacturing selected are as follows:

-) Nepal lube oil ltd (NLOL)
-) Joyti Spinning Mills Ltd. (ISML)
-) Nepal Lever Ltd.(NLL)

3.5 Analytical Tools Used

Financial as well as statistical tools have been used for analyzing capital structure management in Nepalese manufacturing companies.

3.5.1 Financial Tools

The measuring instrument, which can be used in financial analytical is known as financial tools. It helps to calculate the relationship between two financial variables of ratio and percentage basis. Under these analyses, the following calculation are made

Degree of Leverage:

Degree of Operating Leverage (DOL)

$$= \text{Percentage Change in EBIT} / \text{Percentage Change in Sales}$$

Degree of Financial leverage (DFL)

$$= \text{Percentage change in EPS} / \text{Percentage Change in EBIT}$$

Ratio Analysis:

Long Term Debt as percentage of Total Debt

$$= \text{Long Term Debt} / \text{Total Debt}$$

Debt Equity Ratio in terms of Long term Debt and Shareholders Equity

$$= \text{Long Term Debt} / \text{Shareholders Equity}$$

Debt Equity Ratio in terms of total Debt to Shareholders Equity

$$\text{Total Debt} / \text{Shareholders Equity}$$

Debt to Total Assets Ratio:

$$= \text{Total Debt} / \text{Total Assets}$$

Shareholders Equity to Total Assets Ratio

$$= \text{Shareholders Equity} / \text{Total Assets}$$

Profit Margin:

$$= \text{Net Profit} / \text{Sales}$$

Earning After Tax/Number of Shares

Price Earning Ratio (P/E Ratio)

$$= \text{Market Price Per Share} / \text{Earning Per Share}$$

DU-Point Analysis:

Return on Equity (ROE)

$$= \text{Profit margin} * \text{Total Assets Turnover} * \text{Equity Number}$$

OR

$$= \text{Net Profit} / \text{Sales} * \text{Sales} / \text{Total Assets} * \text{Total Assets Equity}$$

Return on Asset (ROA)

$$= \text{Net Profit} / \text{Total Asset}$$

All the necessary calculations and analysis have been made to arrive to the conclusion to the study.

CHAPTER IV

PRESENTATION AND ANALYSIS OF DATA

The objectives of this study have been already emphasis in the introduction chapter. In order to achieve these objectives, several analytical tolls and techniques should be used. The purpose of analyzing the data is to change it from an unprocessed form to an understandable presentation. The collected data need to be aggregated into a form that presents the summary of answers from respondents. The raw data convey title information as such. These must, therefore, be complied, analyzed and interpreted carefully before their full meaning and implication can be understood. The data are thus transformed into information. This process of transforming data is called analysis, examination and interpretation of data to draw conclusions. The general purpose of this chapter is to examine the processes by which the meaning and implications of research data can best the extracted (Wolff & Pant, 1975:247). This chapter is the focal part of the study.

Many studies have been conducted over the last three to four decades on the issue of capital structure. Some indicated that capital structure affects on cost of capital, while others didn't indicate so. Those who advocated that capital structure affect cost of capital are mainly by Barges (1963), Weston (1963), Modigliani and Miller (1966), and Sharma and Ray (1968). Those who advocated that capital structure doesn't affect cost of capital are mainly by Hamada (1972) and Miller (1977).

There are many studies in the field of capital structure and cost of capital in the developed countries. Their applicability is yet to be verified in the context of underdeveloped country like Nepal. For testing the impact of capital structure in the cost of listed manufacturing companies of Nepal,

here empirically analyze the data take form the different two i.e. manufacturing sector and trading sector.

4.1 Descriptive Analysis of Ratios

1. Analysis of Debt to Equity Ratio

To operate or mobilized the company or business, needs a financial resources. And they have to borrowed fund by issuing debenture and issuing shares and it is known as debt equity. The relationship between borrowed funds and owner's capital is a popular measure of the long term financial solvency of a company or firm. This is shown only by the debt-equity ratio. This ratio considers the relative claims of creditors and shareholders against the assets of the firm. The relationship between Debt and equity ratio of the manufacturing companies are presented as follows:

4.2 Analysis of Leverage

The company needs a huge amount of funds for operating its business activities and these funds are collected from various sources having different cost rate. On the way of profitability, the company can use equity capital. In the process of profit planning, it tries to increase the amount of profit but different kinds of leverage are considered. Generally, there are two types of leverage.

) Operating Leverage

) Financial Leverage

The operating leverage refers to the use to fixed charge bearing source for operating the firm, while the financial leverage measures the responsiveness of EPS to the change in EBIT.

4.2.1 Degree of Operating Leverage

Operating leverage is a type of leverage which depends on sales, variable cost and fixed cost. Operating leverage defined as proportion between change in EBIT and change in sales. The operating leverage can be measured as the degree of operating leverage (DOL) in following table. Also it calculate

$$\text{DOL} = \frac{\% \text{ change in EBIT}}{\% \text{ change in Sales}}$$

Jyoti Spinning Mills Ltd

Amount in 000000

Year	EBIT	% Change in EB	Sales	% change in Sal	DOL
1999/00	111.33	-	499.68	-	-
2000/01	168.74	51.57	648.30	29.74	1.73
2001/02	112.82	(33.14)	673.09	3.82	(8.67)
2002/03	94.83	(15.95)	646.74	(3.91)	(4.08)
2003/04	117.88	24.31	725.04	12.10	2.01
2004/05	110.36	(6.37)	718.64	(8.82)	0.722

Unilever Limited

Amount in 000000

Year	EBIT	% Change in EB	Sales	% change in Sal	DOL
1999/00	155.23	-	1503.69	-	-
2000/01	166.47	7.24	1728.63	14.96	0.48
2001/02	127.94	(23.15)	1540.99	(10.85)	2.13
2002/03	73.75	(42.35)	1236.05	(19.79)	2.14
2003/04	133.55	81.08	1244.72	0.70	116.85
2004/05	190.32	42.50	1524.90	22.50	1.89

Nepal Lube Oil Limited

Amount in 000000

Year	EBIT	% Change in EBIT	Sales	% change in Sales	DOL
1999/00	15.94		107.33		
2000/01	10.48	(34.25)	107.19	(0.13)	263.46
2001/02	0.47	(95.57)	72.22	(32.62)	2.93
2002/03	14.21	2923.40	136.01	88.33	33.10
2003/04	11.42	(19.63)	119.15	(12.40)	1.58
2004/05	6.25	(45.27)	84.72	(28.89)	1.56

(Sources Nepal Stock Exchange Limited)

The degree of operating leverage can be measured by the study of EBIT and sales revenue. When sales increases and cost remain same then EBIT also increase. In that time leverage is constant. It effects to change in sales and EBIT. In above table we are calculating DOL in different manufacturing organization. Jyoti Spinning mills in the year 1999, the degree of operating leverage is 1.73 which means 1% change in sales revenue will causes 1.73% change in EBIT. It shows that when sales are increases the profit also increasing rapidly. In year 2000/01, sales are increases but EBIT is decrease the result of DOL (8.67). This means 1% decrease in sales, EBIT is also decrease by 8.67% and that is a cause of losses. In financial year 2004/05, DOL is 0.722 which means 1% change in sales cause 0.72% change in EBIT, it is positive and it is the sign of prosperity. In above financial analysis DOL is negative in two years. It shows that small decrease in sales may be cause of huge loss.

Unilever Limited in the financial year 1999/00 the degree of operating leverage is 0.48 sales is increase in huge EBIT is increase a small amount. It means 1% increase in sales EBIT is increase only 0.48%. In the financial year 2000/01 sales and EBIT is decrease then previous year the operating leverage is 2.13. It means 1% decrease in sales 2.13%

decrease in EBIT. In financial year 2001/02 sales and EBIT also decrease the result of operating leverage is (2.14). It shows that when sales decrease 1% EBIT decrease 2.14%. In financial year 2002/03, sales are increase a small amount but EBIT is increase a huge amount. The result of DOL is 116.85. It means 1% increase in sales 116.85% increase EBIT.

Nepal Lube and Oil Limited, The calculation of DOL shows 263.14. It means when decrease in small amount EBIT is decrease huge amount. In year 2000/01 DOL is 2.93. It shows that 1% sales decrease then 2.93% decrease in EBIT. In year 2001/02 DOL is 33.10. In that situation sales increase only 1% then EBIT increase 33.10%. In year 2002/03 is 1.58. It shows that 1% decrease in sales, 1.58% decrease in sales.

4.2.2 Degree of Financial Leverage (DFL)

Degree of financial leverage measures proportional changes I EPS as a result of change in EBIT. The financial leverage exists when the company has debt capital structure. The degree of financial leverage is calculus and shows in following data. Also it calculate

$$Dol = \frac{\% \text{change in EPS}}{\% \text{Change in EBIT}}$$

Jyoti Spinning Mills Ltd

Amount in 000000

Year	EPS	% CHANGE	EBIT	%CHANGE	DFL
1999/00	(27.10)	-		-	-
2000/01	16.06	(144.50)	168.74	51.57	2.80
2001/02	(22.23)	(284.32)	112.82	(33.14)	8.58
2002/03	(25.93)	(16.64)	94.83	(15.95)	(4.08)
2003/04	117.88	24.31	725.04	12.10	1.043
2004/05	(26.93)	(3.86)	117.88	24.31	(0.1587)

Nepal Liver Limited

Amount in 000000

YEAR	EPS	% CHANGE	EBIT	% CHANGE	DFL
1999/00	129.28		155.23		
2000/01	130.98	1.31	166.47	7.24	0.18
2001/02	73.90	(43.57)	127.94	(23.15)	1.88
2002/03	46.28	(37.37)	73.75	(42.35)	0.88
2003/04	101.19	118.65	133.55	81.08	1.46

Nepal Lube Oil Limited

Amount in 000000

YEAR	EPS	%CHANGE EBIT	EBIT	EBIT	DFL
1999/00	47.61		15.94		
2000/01	25.04	(47.41)	10.48	(35.25)	1.3842
2001/02	(10.89)	(143.50)	0.47	(95.52)	1.50
2002/03	(30.60)	180.99	14.21	2923.40	10.0619
2003/04	(20.60)	31.73	11.73	19.63	1.62

(Source:- Nepal Stock Exchange Limited)

Mentioned in above table the DFL Jyoti Spanning Mills was 2.80 in the financial year 1999/00. EBIT and sales both increase. It shows that 1% increase in EBIT 2.80% change in EPS. In financial year 2000/01 DFL was 8.58%. In year 2001/02 DFL is 1.043. EBIT and EPS also decrease. It means EBIT change in 1% EPS change in 1.043%. In financial year 2002/03 DFL was (0.1587). In this year EBIT increase 24.31% but decrease (3.80). It shows that when EBIT increase 1% EPS decreases 0.1587%.

The calculation of DFL for Uniliver Limited shows it's exactly condition of the company, DFL for the FY 1999/00 is (0.18), FY 2000/01 is 1.88, FY 2001/02 is 0.88, and FY 2002/03 is 1.46. It shows that in year 1999/00 EBIT and EPS both increase when EBIT increase by 1% EPS only increase 0.18% similarly in year 2001/02 EBIT and EPS both decrease, it shows that when the EBIT decrease by 1% EPS also decrease. In year 2000/03 EBIT and EPS both increase. It means that EBIT increase by 1% EPS also increase by 1.46%. In above calculation, the EBIT and EPS for NLL are fluctuating DFL also fluctuates.

The DFL for NLOL in the FY 1999/00 was 1.3842 EBIT and EPS both decreases. The DFL shows that 1% decrease EBIT 1.38% decrease EPS. In FY 2000/01 DFL was 1.50% change in EPS. In FY 2001/02 DFL was (0.0619) EBIT was increase but EPS was decrease. The result shows that 1% increase in EBIT 0.069% decrease in EPS. In FY 2002/03 DFL was 1.62 EBIT and EPS both increase. The result show that 1% change in EBIT cause 1.62% change in EPS. The NLOL, DFL and EPS and EBIT are very fluctuates.

In the capital structure of any company, interest expenses and return on equity increase the level of financial position. According to the calculation of DFL the selected manufacturing companies do not shows any positive signal. None of the companies DFL has consistency. Therefore companies should change their capital structure.

4.2.3 Long Term Debt as a Percentage of Total Debt

Long term debt is a percentage of total debt shows the proportion of Long-Term Debt (LTD) and the total debt of the company. The calculation of LTD is presented in the following table.

Jyoti Spinning Mills Ltd

Amount in 000000

Year	Long term Debt	Total Debt	EBIT
1998/99	429.74	873.44	0.492009
1999/00	408.63	891.77	0.458224
2000/01	393.54	884.22	0.44507
2001/02	529.47	868.52	0.609623
2002/03	573.74	863.41	0.664505

Unilever Limited

Amount in 000000

Year	Long term Debt	Total Debt	EBIT
1998/99		267.72	
1999/00		263.93	
2000/01		354.32	
2001/02		223.21	
2002/03		426.45	

Nepal Lube Oil Limited

Amount in 000000

Year	Long term Debt	Total Debt	EBIT
1998/99	17.71	59.01	0.290968
1999/00	34.80	81.26	0.428255
2000/01	36.26	74.27	0.488219
2001/02		66.15	
2002/03		93.96	

Source:- Nepal Stock Exchange Limited)

For Jyoti Spinning Mills the LTD as a percentage of TD is 49.20% in FY 1998/99. In this year LTD is half to the TD. In Financial year 1999/00 the long term debt is decreasing and total debt is increasing the result LTD as a percentage of TD is also decrease in financial year 2000/01 the long term debt is decreasing and total debt is also decreasing. The result long-term debt as a percentage of total debt is 44.05%. The LTD as a percentage of total debt is decreasing order. It shows that long term debt also decreasing order. In financial year 2001/02 the long term debt is increase and total debt is decrease and result is also LTD as a percentage of total debt was 60.96% in financial year 2002/03 the long term debt is increase and total debt is decrease. Long term debt as a percentage of total debt is 66.45%. In last two years long term debt as a percentage of total debt is increasing.

From the analysis of the data of Unilever Limited it is clear that the LTD is Nil from five year. But the total debt is 267.72 in FY 1998/99, 263.93 in FY 1999/00, 354.32 in FY 2000/01, 223.21 in FY 2001/02, 426.45 in FY 2002/03. In that shows that Unilever used only a short term liabilities the company do not use long term loan in that five year. From the analysis of the data Nepal Lube and Oil Limited is Nil from last two years. This company use only short sources. In beginning three years the company long-term debt as a percentage is 29.09%, 42.82%, 48.81% respectively, in financial year 1998/99, 1999/00, 2000/01. The long term debt is increasing order and the result percentage of total debt is also increasing.

Normal total debt is composed by two debts one is long term debt and another is short-term debt. Long term debt is use for a long period while short term debt use only for one year and less.

4.2.4 Debt-Equity (DE) Ratio in Terms of Long Term Debt

This ratio is calculating the proportion between long term debt and shareholders equity. That can be analyzing the DE ratio of the firm. The following table shows that the calculation of debt equity ratio in terms of long term debt and shareholders equity.

Jyoti Spinning Mills Ltd

Amount in 000000

Year	Long term Debt (LTD)	Shareholders Equity (SE)	LTD/SE
1998/99	429.74	(98.63)	(4.357)
1999/00	408.63	(83.63)	(4.8861)
2000/01	393.54	(93.09)	(4.227)
2001/02	529.47	(69.01)	(7.6723)
2002/03	573.74	(81.55)	(7.0354)

Unilever Limited

Amount in 000000

Year	Long term Debt (LTD)	Shareholders Equity (SE)	LTD/SE
1998/99		250.40	
1999/00		324.94	
2000/01		342.35	
2001/02		348.13	
2002/03		358.43	

Nepal Lube and Oil Limited

Amount in 000000

Year	Long term Debt (LTD)	Shareholders Equity (SE)	LTD/SE
1998/99	17.71	37.66	0.455921
1999/00	34.80	39.34	0.884596
2000/01	36.26	37.14	0.976306
2001/02		38.60	
2002/03		39.70	

Sources: Nepal Stock Exchange Ltd

For Joyti Spinning Mills (JSM) DE ratio is calculated by using long term debt and shareholder equity, which is in fluctuating trend. The JSM has negative shareholder equity. The company statement shows drastic loss in past few years. The losses don't cover its share capital, so shareholder equity is negative. The company is using a high amount of debt in that condition of loss. Therefore the company should try to reduce its debt by any available resources to solve with this problem.

For Unilever Ltd the DE ratio is not available in the study period. The company did not use long term debt. The company is levered company. Company financed of its all capital through only equity capital.

The DE ratio for Nepal Lube and Oil Limited (NLOL) is calculating by using long term debt and shareholders equity. In first three years the DE ratio are 45.59%, 88.46% and 97.63% in the financial year 1998/99,1999/00 & 2000/01 respectively. In the last two years long term debt did not use the company.

Those companies who are not using debt in their capital structure will have to pay a large amount as tax as they don't get the opportunity of tax benefit on interest that will definitely decrease their profit also. The JSM is using excess amount of debt, which is the worst financial condition. So it is necessary to keep proper balance to both debt and equity for the betterment of their performances and optimal capital structure.

4.2.5 Debt to Total Assets Ratio (D/A Ratio)

This ratio established a relationship between total debt and total assets. The ratio indicates the proposition of contribution and the purchase of total assets by the creditors and owners. It is computed by dividing the total debt by total assets. A higher D/A ratio indicate that the creditors have the greater claim an total assets than the owners, it also indicates

that firms financial risk is high and vice versa. The debt to total assets ratio for the selected manufacturing companies is calculate and presented the following table.

Jyoti Spinning Mills Ltd

Amount in 000000

Year	Total Debt (TD)	Total Assets (TA)	TD/TA
1998/99	873.44	839.85	1.040
1999/00	891.77	875.27	1.018
2000/01	884.22	859.46	1.029
2001/02	868.52	788.58	1.101
2002/03	863.41	772.28	1.118

Unilever Ltd

Amount in 000000

Year	Total Debt (TD)	Total Assets (TA)	TD/TA
1998/99	267.72	544.81	0.4914
1999/00	263.93	629.75	0.4191
2000/01	363.21	760.34	0.4779
2001/02	223.21	571.34	0.3906
2002/03	426.45	784.91	0.5433

Nepal Lube and Oil Ltd

Amount in 000000

Year	Total Debt (TD)	Total Assets (TA)	TD/TA
1998/99	59.01	101.20	0.5831
1999/00	81.26	126.05	0.6446
2000/01	74.27	117.18	0.6338
2001/02	66.15	111.83	0.5915
2002/03	93.96	143.33	0.6217

(Sources: Nepal Stock Exchange)

Debt to Total Assets of Joyti Spinning Mills in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 is 1.04, 1.081, 1.029, 1.101 and 1.11 respectively. The average D/A ratio are 1.06 in the study period. The ratio shows that the assets are financed through only with debt. The situation of the company is dangerous; the proportion of the debt is higher than the assets. Every financial year the proportion of the debt is more than 50% of that correspondent year.

For Unilever Ltd, the Debt to total assets ratio is fluctuated. The D/A ratio is 49.14, 41.91, 47.80, 39.07 and 54.33 percent in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. The average ratio of the research period is 46.45%, which shows that 46.55% of the total assets financed by the debt. That can be a good side of Unilever.

For Nepal lube and Oil Ltd the Debt to total assets ratio is 58.31%, 65.46%, 63.38%, 59.15%, 62.17% in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. The average ratio of the company is 62.17%, which shows the more of the assets financed by the debt capital like Jyoti Spinning Mills. This is very dangerous.

4.2.6 Shareholders Equity to Total Assets Ratio

This ratio is established the relationship between shareholders' equity and the total assets. It is calculated by dividing share equity to total asset ratio inform as about the proportion of total assets of the company financed by the ownership capital which is shown in the following table.

Jyoti Spinning Mills Ltd

Amount in 000000

Year	Shareholders equity (SE)	Total Assets (TA)	SE/TA
1998/99	(98.63)	839.85	(0.1174)
1999/00	(83.63)	875.27	(0.0955)
2000/01	(93.09)	859.46	(0.1083)
2001/02	(69.01)	788.58	(0.0875)
2002/03	(81.55)	772.28	(0.1055)

Unilever Ltd

Amount in 000000

Year	Shareholders equity (SE)	Total Assets (TA)	SE/TA
1998/99	250.40	544.81	0.45961
1999/00	324.94	629.75	0.5159
2000/01	342.35	760.34	0.4502
2001/02	348.13	571.34	0.6093
2002/03	358.43	784.91	0.4566

Nepal Lube and Oil Ltd

Amount in 000000

Year	Shareholders equity (SE)	Total Assets (TA)	SE/TA
1998/99	37.66	101.20	0.3721
1999/00	39.34	126.05	0.3120
2000/01	37.14	117.18	0.3168
2001/02	38.60	111.83	0.3451
2002/03	39.70	143.33	0.2769

(Sources: Nepal Stock Exchange)

For JSM the entire ratio are negative due to negative shareholders' equity. The ratio is (0.1174), (0.0955), (0.1083), (0.0875) and (0.1055) for the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. The average SE/TA ratio is (0.1028). The SE/TA ratio

shows that the total assets financed by only debt because the shareholders equity capital is negative. There is no any involvement of equity capital for the financing its assets. So, the company is in risk of liquidation at any time.

For Unilever, the calculation of ratio between shareholders equity and total assets is fluctuated. The shareholders equity and total assets are 45.96, 51.59, 45.02, 60.93 and 45.67 percent in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. This means 45.96% total assets financed by the equity capital in year 1998/99 and so on. The average SE/TA ratio is 49.83%. This tells us that in average the input of equity for the assets is 49.83%.

For NLOL, SE/TA ratio is constant than other companies. The ratio is 37.21%, 31.20, 31.68, 34.51 and 27.69 percent in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. The SE/TA ratios shows that 37.21% of total assets financed by equity capital, 31.20% of total assets financed by equity capital in year 1998/99, 1999/00 and so on.

4.2.7 Interest Coverage Ratio:

The interest coverage ratio is calculated with the help of profit and loss account of company by which the company can analyze its own capability for the payment of fixed charges. Coverage ratio is one of the parts of capital structure and leverage ratio.

Interest coverage ratio is a part of coverage ratio, which is calculated and presented in the following table.

Jyoti Spinning Mills Ltd

Amount in 000000

Year	EBIT	Interest Charge	EBIT/Int
1998/99	111.33	112.15	0.9896
1999/00	168.74	115.38	1.4624
2000/01	112.82	104.42	1.080
2001/02	94.83	104.83	0.9046
2002/03	117.88	82.73	1.4248

Unilever Limited

Amount in 000000

Year	EBIT	Interest Charge	EBIT/Int
1998/99	155.23	10.12	15.3389
1999/00	166.47	3.84	43.3515
2000/01	127.94	14.21	9.0035
2001/02	73.75	12.61	5.848
2002/03	133.55	2.60	51.36

Nepal Lube and Oil Ltd

Amount in 000000

Year	EBIT	Interest Charge	EBIT/Int
1998/99	15.94	2.63	6.060
1999/00	10.48	3.32	3.1566
2000/01	0.47	3.84	0.1223
2001/02	14.21	3.68	3.8614
2002/03	11.42	3.01	3.7940

(Sources: Nepal Stock Exchange)

The situation of JSM in the financial year 1998/99 interest coverage ratio is 0.9896. It shows that the company has not strong position. Then

company does not able to pay interest for this profit. The situation of the company is very poor. In the financial year 1999/00 company EBIT is increase in this situation company situation has little improve. Interest coverage ratio is 1.4624. Company has paid interest for his profit. In financial year 2000/01 EBIT is decrease, interest coverage ratio is 0.9046; company situation is going to bad, it has gone boundary line. In financial year 2002/03 the interest coverage ratio is 1.42. The ratio is above boundary line. The company paid to his interest for this profit.

For Unilever, the EBIT is sufficient to repay its interest charges except for the financial year 2000/01. When the profit is very nominal but the interest charge is still growing. The ratios are 6.060, 3.16, 0.12, 3.86 and 3.80 times for the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively.

For NLL, the interest coverage ratio is strong position. In study period the ratio is much fluctuated. The EBIT is sufficient to repay its interest charge. The ratios are 15.34, 43.35, 9.003, 5.85, and 51.36 times for the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. From the above calculation the company is sufficient to repay the interest charge. In financial year 1998/99 ratio is 15.34 then the ratio is highly increase then after the ratio is decrease but the final year the ratio is very increase. For the creditors point of view NLL is very safety due to this coverage ratio.

4.2.8 Profit Margin

Profit is the main objective for any business organization. The company find outs its profitability with the help of profit margin ratio. The profit is directly related to the sales revenue of the company. When sales volume is increase profit also increase. Profit margin is calculated by profit and

sales revenue profits margin is proportion between Net Profit and sales revenue. The following table shows the profit margin.

Jyoti Spinning Mills Ltd

Amount in 000000

Year	Net Profit	Sales	NP/Sales
1998/99	(36.33)	499.68	(0.0727)
1999/00	16.16	648.30	0.0249
2000/01	(29.91)	673.09	(0.0444)
2001/02	(50.27)	646.74	(0.0777)
2002/03	(52.92)	725.04	(0.0729)

Unilever Ltd

Amount in 000000

Year	Net Profit	Sales	NP/Sales
1998/99	119.03	1503.69	0.07915
1999/00	120.59	1728.63	0.06967
2000/01	68.04	1540.99	0.04415
2001/02	42.61	1236.05	0.03447
2002/03	93.71	1244.72	0.07485

Nepal Lube and Oil Ltd

Amount in 000000

Year	Net Profit	Sales	NP/Sales
1998/99	9.66	107.33	0.09003
1999/00	5.08	107.19	0.047392
2000/01	(2.21)	72.22	(0.0306)
2001/02	6.21	136.01	0.04565
2002/03	4.24	119.15	0.03558

(Sources: Nepal Stock Exchange)

The profit margin for Jyoti Spinning Mills during the study period is negative except financial year 1999/00. The margin ratio is (7.22), 2.49, (4.44), (7.78) and (7.30) percent in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. In financial year 2000/01 the sales revenue is increase but the profit is decreased. It means the company did not use his resources properly. In same case in financial year 2002/03 sales revenue is increase but net profit is negative because profit margin in negative. In above calculation we can sales volume is not fluctuated vastly, but the company is gone loss. It indicates that the capital structure of the company is not suitable and the company is not using its resources properly. The average profit margin ratio is also negative. It indicates the very poor condition of the company. For NLL, sales volume is fluctuated. In financial year 1998/99 profit margin is 7.91%. It shows that the company is in smooth condition. In financial year 1999/00 the sales volume is increased and the net profit is also increased but the profit margin is decreased. The reason of decrease due to company did not use its resources properly. In financial year 2000/01 the sales revenue and the profit is decreased because the profit margin is also decreased cause of decreased in profit margin. In financial year 2002/03 the sales revenue and net profit both are increased similarly profit margin also increase. Calculation of above table it shows that the financial year 1998/99 is the best year from the point of view of profit margin ratio of the company. The fluctuated situation of the company tell us about the inefficiency on smooth running of the business, which management of the company should try to eliminate such problem for success in the long run.

For NLOL the profit margin is 9%, 4.73%, (3.06%), 4.57% and 3.65% in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03

respectively. The profit margin ratio of NLOL is fluctuating, in financial year 2000/01 the company suffered loss. Calculating the above table it shows that the financial year 1998/99 is the best year from the point of view of net profit and profit margin. But in financial year 2001/02 is the best year from the point of view of sales revenue.

The overall calculation shows that the net profit is fluctuating and profit margin ratio is also decreasing whereas the sales revenue is increased. This indicates that the company should make such policy to earn high amount of profit from the sales revenue by increase by increase operating efficiency.

4.2.9 Earning Per Share (EPS)

EPS means the return of the shareholders from their investments. EPS measures earning available to shareholder on per share basis, EPS is proportion between net profit and No. of share. The following table shows the EPS for the selected manufacturing company.

Jyoti Spinning Mills Ltd

Amount in 000000

Year	Net Profit	NoS	NP/NoS
1998/99	(36.33)	134.04	(27.10)
1999/00	16.16	134.04	12.06
2000/01	(29.91)	134.04	(22.23)
2001/02	(50.27)	193.84	(25.93)
2002/03	(52.92)	193.84	(26.93)

Unilever Ltd

Amount in 000000

Year	Net Profit	NoS	NP/NoS
1998/99	119.03	92.07	129.28
1999/00	120.59	92.07	130.98
2000/01	68.04	92.07	73.90
2001/02	42.61	92.07	46.28
2002/03	93.71	92.07	101.19

Nepal Lube and Oil Ltd

Amount in 000000

Year	Net Profit	NoS	NP/NoS
1998/99	9.66	20.29	47.61
1999/00	5.08	20.29	25.04
2000/01	(2.21)	20.29	(10.89)
2001/02	6.21	20.29	30.60
2002/03	4.24	20.29	20.89

(Sources: Nepal Stock Exchange)

For the JSML, its condition is very good among the selected companies. In 5 years financial period except 1999/00 the company has gone loss. In general condition EPS cannot negative. The EPS are (27.10), 12.06, (22.23), (25.93) and (26.93) percent in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. The calculation shows that except 1999/00 the shareholders of the company are not getting anything from their investments. The average EPS for the company is also negative that tell us about the most difficult situation of the company.

For Unilever, the condition is quite satisfactory among the selected company for the study. The EPS are 129.28%,130.98%,73.90%,46.28%

and 101.19% in financial year 1999/00, 2000/01, 2001/02 and 2002/03 respectively. So this indicates that EPS 96.93% that is good condition for the shareholders. So shareholders are getting 96.33% return from their investments. Therefore the company should try to give more return to shareholders by increasing its capacity to maximize its profit.

For NLOL, the EPS are fluctuating due to fluctuation of net profit. The EPS are 47.61%, 25.04%, (10.89%), 30.60% and 20.89% in financial year 1999/00, 2000/01, 2001/02 and 2002/03 respectively. The above calculation shows that financial year 1998/99 is the best for the point of view of net profit and EPS. In that year shareholders are getting more return among the research period. The average EPS is 22.65%, so shareholders are getting 22.65% return from their investment in research period. Therefore the company should try to give more return to shareholder by increasing its capacity to maximize profit. Then company should make a good policy to solve with this problem.

The EPS and the net profit are directly related. When net profit is increased the EPS also increase. Therefore the company should attain towards their operation to earn amount of profit.

4.2.10 Profit Earning Ratio (P/E Ratio)

P/E Ratio indicates the times of earning per share are covered by its market price. The P/E ratio represents the amount which investors are willing to pay each rupees of the earning. The calculation of P/E ratio for the company selected for the study is presented in the following table.

Jyoti Spinning Mills Ltd

Amount in 000000

Year	MPS	EPS	P/E Ratio
1998/99	44.00	(27.10)	(1.6236)
1999/00	44.00	12.06	3.64
2000/01	43.40	(22.23)	(1.93)
2001/02	26.38	(25.93)	1.02)
2002/03	31.00	(26.93)	(1.15)

Unilever Ltd

Amount in 000000

Year	MPS	EPS	P/E Ratio
1998/99	1501	129.28	11.61
1999/00	2230	130.98	17.03
2000/01	2200	73.90	29.77
2001/02	1350	46.28	29.17
2002/03	1130	101.19	11.17

Nepal Lube and Oil Ltd

Amount in 000000

Year	MPS	EPS	P/E Ratio
1998/99	300.00	47.61	6.30
1999/00	420.00	25.04	16.78
2000/01	584.00	(10.89)	(53.63)
2001/02	480.00	30.60	15.686
2002/03	400.00	20.89	19.15

The P/E Ratio of JSML all of except 1999/2000 all the year negative cause P/E ratio is also negative. The P/E ratio is also negative. The P/E ratios are (1.62), 3.64, (1.93), (1.02), and (1.15) in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. In the year 2000/2001 and 2001/2002 is MPS is not available, it is assumed that

from the trend of NEPSE. This P/E ratio informs us that shareholders will losses if they sell their shares at the prevailing market price. The P/E ratio indicates bad situation of the company.

For Unilever, the P/E ratio are 11.6%, 17.03%, 29.77%, 29.11%, 11.17% in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. In the initial period the P/E ratio is increased but after 2001/02 the P/E ratio decreased. The market price of the share is fluctuated and also earning per share also fluctuated. The P/E ratio of the company for the financial year 1998/99 is 11.6%, which means that the investors can earn 11.61 times then the EPS, if they sell their share at the market price. Similarly investors can earn that much time as per its P/E ratio when they sell their shares at the market price for other four years study period. The trend of P/E ratio indicates the bright future of the company so investors should have to confidence not to sell their shares.

For NLOL, the P/E ratio for the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 are 6.30, 16.70, (53.63), 15.68 and 19.15 respectively.

The P/E ratio for 1998/99 shows the investors can earn 6.3 times than EPS, if they sell their share at the market price. Except year 2000/01 the investors can earn that times as per its P/E ratio when they sell their at a market price. The P/E ratio of financial year 2000/01 is in negative. In that situation shareholders will be benefited if they sell their shares at the market price.

4.3 Dupont System Analysis

The Dupont system of ratio is widely used by the financial manager to make classified assessment of firm's profit margin. Total assets turnover ratio and equity multiplier. It also shows various activities by which these

ratios interact to determine profitability. Dupont system helps to find out the causes of changing ROE, ROA and profit margin.

4.3.1 Return on Equity

The profit of Shareholders' from their investments is calculated by return of on equity, it can be used as a measuring rod of companies from the point of view of the investors. It can be calculated by using the following formula.

$$\begin{aligned} \text{ROE} &= \text{Profit margin} * \text{Total assets turnover} * \text{Equity multiplier} \\ &= \frac{\text{Net profit}}{\text{Sales}} * \frac{\text{Total assets}}{\text{Total Assets}} * \frac{\text{Total assets}}{\text{Equity}} \end{aligned}$$

The following table shows the calculation of ROE for the selected company for the study

Jyoti Spinning Mills Ltd

Year	Profit margin %	Total Assets Turnover	Equity Multiplier	ROE%
1998/99	(7.27)	0.59	(8.52)	36.89
1999/00	2.49	0.74	(10.47)	(19.32)
2000/01	(4.44)	0.78	(9.23)	32.13
2001/02	(7.77)	0.82	(11.43)	72.83
2002/03	(7.30)	0.9724	(9.48)	67.32

Nepal Leaver Limited

Year	Profit margin %	Total Assets Turnover	Equity Multiplier	ROE%
1998/99	7.92	2.76	2.18	47.54
1999/00	6.98	2.74	1.94	37.11
2000/01	3.45	2.03	2.22	19.87
2001/02	3.45	2.16	1.64	12.22
2002/03	7.439	1.59	2.19	26.080

Nepal Lube and Oil Limited

Year	Profit margin %	Total Assets Turnover	Equity Multiplier	ROE%
1998/99	9.0	1.06	2.69	25.65
1999/00	4.74	0.85	3.20	12.91
2000/01	(3.06)	0.62	3.16	(5.95)
2001/02	4.57	1.22	2.90	16.17
2002/03	3.56	0.82	3.61	10.54

(Source: -Appendix table no 12&13)

The position calculated in the above table shows that the situation of JSML is worst among the selected companies for research. The assets from over ratio shows that the company is enable to use its assets efficiently as the entire ratio shows the value less than one. Almost all the ratios are in the negative sign. The ROE for financial 1998/1999, 1999/00, 2000/01, 2001/02, and 2002/03 are 36.86, (19.33) 312.13, 72.83, 76.32, respectively Most of the ratios are negative and some of the are positive due to the double negativity which is not satisfactory for the company. The management of the company is advice rearrange its capita structure and run the company with a new side.

For NLL the ROE are 47.54, 37.11, 90.87, 12.22 and 26.08 in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. The starting year, the ROE is decline and last year the ROE is increasing also the assets turnover is decreasing Trend and the equity multiplier is fluctuating trend as the shareholder equity is vibrating, which shows the equity value is also fluctuating is asset financing due to the above reason the ROE for the company also irregular. The average ROE is 28.564, which is highest ROE among the selected company.

For the NLOL profit margin, total assets turnover, equity multipliers are fluctuation trends. In the financial year 2000/01 profit margin and ROE is negative. The ROE are 25.65%, 12.91% ,(5.95)%16.17% and 10.54 in the year1998/99, 1999/00, 2000/01, 2001/02and2002/03 respectively. The average ROE is 11.86% for the company, which is not so bad during the present position. But ratio is declining for which NLOL should try to treat the weak before it becomes worst. In the financial year 1998/99 the ratio is highest, which reveals the fact that shareholders return during this year. The profitability as well as production power of assets in terms of generating sales is measured by the ROA. The relationship between net profit and total assets is analyzed by 'ROA. The following table the ROA for the manufacturing companies listed in NEPSE selected for the study.

Jyoti Spining Mills

Year	Net Profit	Total Assets	NP/TA
1998/99	(36.33)	839.85	(4.33)
1999/00	16.16	875.27	1.85
2000/01	(29.91)	859.58	(3.48)
2001/02	(50.27)	788.58	(6.37)
2002/03	(52.21)	722.98	(6.75)

Nepal Leaver Limited

Year	Net Profit	Total Assets	NP/TA
1998/99	119.03	544.81	21.85
1999/00	120.59	629.75	19.15
2000/01	68.04	760.42	8.95
2001/02	42.61	571.34	7.46
2002/03	93.17	784.91	11.87

Nepal Lube Oil Limited

Year	Net Profit	Total Assets	NP/TA
1998/99	9.66	101.20	9.55
1999/00	5.08	126.05	4.03
2000/01	(2.21)	117.18	(1.89)
2001/02	6.21	111.83	5.55
2002/03	4.24	143.33	2.96

(Source:- Appendix table no 9&7)

For the JSML the ROA are (4.3) %, 1.83% , (6.37) %,(6.75)% in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. The average ROA is during the entire period is (3.82) %. The company has a maximum amount of assets among the selected companies. But the profit of the companies is negative. The capacity of the company assets in the term of the generating sales. Earning net profit is very weak, which indicates the inefficient productivity of the assets. The statistics relation to JSML is extremely horrifying, as net profit of the company is negative sign.

In the case of NLL ROA are 21.85%, 19.15%, 8.95%,7.46% and11.87% in the in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. The ROA of NLL is decreasing tend in the fist four year and in the last year the ROA is increase. The average ROA is 13.85%, which is quite among the selected companies.

In the case of NLOL ROA is fluctuating trend, in the financial year2000/01, the ROA is negative. The ROA are 9.55%, 4.03%, (1.89)%, 5.55%, 2.69% in the in the financial year 1998/99, 1999/00, 2000/01, 2001/02 and 2002/03 respectively. The average ROA during entire period is 4.04, which is not satisfactory. Therefore the company most focuses its

strategies to stop the reducing capacity of the assets in the term of the generating sales earning net profit.

4.4 Major Findings of the Study

A summary of the overall calculation for the selected manufacturing companies for the research listed NEPSSE is presented in the following table.

S .N	Ratios	JSML	NLL	NLOL
1	DOL	(2.25)	30.4	75.268
2	DFL	1.66	1.10	1.11
3	LTD to total Debt	0.53	0.00	0.40
4	Debt to Equity	(5.653)	0.00	0.77
5	Debt to total Assets	1.06	0.4645	0.6217
6	Shareholders Equity To total Assets	(0.10284)	0.4983	0.3246
7	Interest Coverage	1.172	24.98	3.3988
8	Profit Margin	(0.04858)	0.06047	0.0376
9	Return on Equity	37.958	28.56	11.86
10	Return on Assets	(3.82)	13.85	4.05
11	Earning per share	(18.26)	96.326	22.65
12	Price Earning	(0.41472)	19.75	0.875

(Source:-average from all ratios)

) Average DOL for JSML is negative, which shows the inefficient earning of the firm. In the case of NLL and NLOL is a positive DOL. For NLOL and NLL, DOL is higher, which shows the risky ness of the company. The NLL & NLOL should try to manage its DOL, whereas JSML should try to increase their sales volume to improve operating position of the company due to negative DOL.

-) The average DFL of JSML, NLL & NLOL is higher than one. JSML has higher DFL among all the companies. There is no any consistency in the DOL for the same type of manufacturing industry.
-) Debt-equity ratio for JSML is positive. The JSML & NLOL is a levered firm but NLL has not long-term debt. So NLL is unleveled firm.
-) Average-debt to total assets ratio for JSML is the highest among selected companies for study. The average ratio is above 50%, all of the studied companies are above the average ratio. This situation indicates that the debt amount is comparatively high for assets financing as per the figure of the ratio.
-) The average ratio between shareholders equity & total assets for JSML is negative value of shareholders equity. This indicates that all the assets have financed out of debt capital, which is not good. The NLOL & NLL have the ratio below 50%, which indicates that more than 50% assets are financed through outsiders' found.
-) The average interest coverage ratio is positive, the NLL has very good coverage ratio, NLL has manageable coverage ratio, but JSML has poor coverage ratio.
-) The profit margin of the company doesn't show the satisfactory figure during the study period. The average ratio is the negative for the JSML; the company is occurring loss during all the study period. The profit margin for NLL is quite good than other studied companies.
-) The ROE for NLL is the highest. The investors of the NLL are getting more return from their investment. For JSML, ROE is

positive due to double negative, it is not so good. The ROE for NLOL is good than JSML.

-) The average return on assets for JSML is negative, which indicates that the assets of this company are not generating profit. The average ROA for NLL is highest, indicating the good production power of assets. The NLOL average is good than JSML.
-) The earning per share for NLL seems to highest among the three companies, so the investor can be attracted by proposal if NLL. The earning per share for JSML is negative indicates the worst situation of the company. The EPS for NLOL is positive but it is poor than NLL.
-) The average P/E ratios are (0.41472), 19.75 & 0.857 for JSML, NLL & NLOL respectively. The higher value of P/E ratio indicates the greater confidence of investors with its future. In the selected companies NLL has the highest value of the P/E ratio.
-) In above calculation shows that the capital structure of three companies, the JSML
-) Company is very poor & NLL condition is better than other two companies.

CHAPTER V

SUMMARY, CONCLUSION AND RECOMMENDATION

5.1 Introduction

This study enquires upon the capital structure management of three selected Manufacturing companies of Nepal. It covers the period of five years from 1998/99 To 2004, 2003 A.D. It includes the data of three manufacturing companies listed with Nepal stock exchange Ltd. Katmandu, Nepal (NEPSE). This chapter summarizes the whole study, draws the major findings, conclusion and forwards the recommendation for the best capital structure management of Nepalese manufacturing companies.

5.2 Summary

Nepal is a land lock country, which is between two countries, China and India. Nepal is a developing country; more than three-fourth of the total land area is hills and mountains. This reason behind Nepalese's underdeveloped economy is not due to lack of resources but it is due to not proper utilization of the available resources in an efficient manner. Nepalese economy is mainly based on agriculture. Without industrialization, development is impossible; the main source of economic development is industrialization. Industrialization helps to uplift the economic standard of the people by creating more employments, earning foreign currency through import substitution and export promotion. Funds are the most important sources to operate the business; generally, the required funds are raised by two sources: equity capital and debt capital. The composition of these two funds is known as capital structure. The term capital structure refers to the proportion of long-term sources of funds such as debenture, long-

term debt preferences share capital and equity capital including reserves and surpluses. Capital structure decision is one of the most important decision that taken by financial manager the optimum capital structure of combinations of the firm.

The capital structure has many relevant dimensions the financing mix is of them other dimensions involve the investments decision of the firm and the optimal use of leverage, with in the constrains imposed by the internal and External environment condition the conceptual framework, different view for different writers, books and journal has been defaulted in the review of literature section. As per the objectives of this study, it tries to analyzes the relationship between debt and shareholders equity of manufacturing companies to provide suggestion are the basis of findings to fulfill this Purpose, the study follows the analytical and descriptive research design. Research methodology is studied in the third chapter. It has included the research design. It presents nature and sources of data, data collection and processing technique and financial tools used. Presentations and analysis of data is studied in the fourth chapters.

AVERAGE D O L for JSML is Negative but NLOL, and NLL is positive DOL. The average DFL is positive for three companies for JSML. NLL is not long term debt in that reason long-term debt to total debt ratio is Nil. Debt to equity ratio for JSML is more than Assets. The average shareholders equity to total assets ratio is negative for JSML. NLOL and NLL ratio are less than 50%. The average interest coverage ratio are 110172, 24.98, 3-3988 for the JSML, NLL and NLOL reactively. The profit margin of the companies does not show a satisfactory picture during the study period.

The average ratio is negative for the JSML, as the company occurring from the losses during glasnost all the study period. The profit margin for

the NLL is highest among the studies companies. The average ROE are 37.958 %, 28.56 % 11.86 % for JSML, NELL and NLOL respectively. The ROE for JSML is positive we to the double negative. The average return an asset for the JSML is negative. The average ROA is highest for NILL among the selected companies the average earning per share in negative for JSML and highest EPS for NLL among the selected companies. The average P/E ratio is negative for JSML and highest P/E ratio fro NLL among the studies companies.

5.3 Conclusion

The average DOL for JSML is (2.25) NLL is 30.4 and NLOL is 75.28 , among the same type of manufacturing companies, there is a vast different in the dol. JSML has the negative DOL, NLL and NLOL has the highest degree of operating leverage which is also harmful for the good health of the company. When the company has high degree of operating leverage, a small change is sales makes a comparatively a high change is EBIT. The average DFL is higher than 1. There is no any constituency is the DOL and DFL for the same type of manufacturing companies. There fore companies should concentrate on restricting their structure of capital. The LTD for JSML is fluctuating position, for NLL ltd is not taken, for NLOL is increasing for the first three year and last two year ltd is not taken. The total debt is fluctuating order for all studies companies. The average de ratio in terms of ltd and shareholder equity for JSML is (5,635). For NLL is nil and For NLOL is (.277). NLL is not using debt in their capital structure, so will have to pay large amount of as tax as, it don't get opportunity of tax benefit so interest, that will surly decrease their profit also. For j is use excess amount of debt, which is harmful to their financial health, so it is necessary to keep proper balance to both of things for the betterment of their performance. For JSML shareholder

equity is negative, because their loss is excess than his share capital, the JSML should try to increase the amount of equity for their capital to be in safer mode against the threat of insolvency.

The average debt to total assets ratio are (1.08), 0.4644 and 0.6217 for JSML, NLL and NLOL respectively. For JSML total debt to total assets ratio is more than one which indicates debt is more than assets. There is no involvement of equity capital for financing its assets, which keeps the company, is risky to liquidation at any time. For NLL it is better than JSML. Its average ratio is 0.4644 which indicates that debt capital is financing 46% to purchase total assets. For NLOL the average ratio is 62 % which shows that total debt is financing 62 % purchase assets. The average shareholder equity to total assets ratio are (.1028), 0.4983, 3246 for JSML, NLL&NLOL respectively. JSML is negative SETAR. There is no any involvement of equity capital for financing its assets. The company should not totally depend of outsider for financing its assets, which keeps the company in risk of liquidation at any time. The average ratio for NLL is 49.83 % which shows that on average the input of equity for the assets if 49.83%.For NLOL the average ratio is 32.46% which means the equity capital financing to assets is 32.46%.

The average interest coverage ratio are 1.172, 24.98 &3.39 times for JSML, NLL,and NLOL respectively. For the JSML ratio is very poor, EBIT is also fluctuating trend. Than the company is not sufficient to repay the interest for 1998/99 and 2001/02. Which is not satisfactory. During the study period the company uses a huge amount of debt to comparisons to its profit. The company should try to manage its debt in relationship its profit. For NLL interest coverage ratio is fluctuating trend. The average ratio is 24.98. The profit is sufficient to repay their interest.

For NLOL, the EBIT is sufficient to repay its interest charge except 2000/01, where the profit is very national but the interest charge is increase. The average profit margin ratio for JSML, is (.04858), all of the study period except 1999/2000 profit margin is negative its shows that the company gone huge losses or the company is not using its resources properly. The ratio is including worst condition of the company. The average profit margin for NLL is 0.06047. The sales volume, net profit margin is fluctuating trend. For the profit point of view NLL is the best among the researcher company. The fluctuating situation of the company management should care about this problem. The average profit margin ratio is 0.0376. All the study period except 2000/01 the ratio is positive and profit, sales is fluctuating trend.

Average ROE for the company are 37.958, 28.56&11.85 for JSML, NLL&NLOL respectively. The JSML ROE is positive due to double negative. For the investor point of view, no one investor can invest to JSML stocks. The return is negative for the study period. The average ratio for NLL is the best for study companies. The investors are getting more returns from their investment. The average ROE for NLOL is good. IT is positive of r investors.

The average ROA is highest for NLL. It is indicating the good production power of assets. But the ROA for JSML is negative, which shows the poor power of assets. The average ROA for NLL is good. Earning per share for NLL seems to be higher than other two companies, so the investors can be attracted by the proposal of NLL, JSML EPS is good.

The higher P/E ratio indicates the grater confidence of investors with its future. The NLL has the higher value of the P/E ratio among the studies company. For JSML P/E ratio is negative. It shows that worst condition of the company. For NLOL except 2000/01 the P/E ratio is positive.

Bibliography

Books:

- Bajracharya, B.c. (2000). Business Statistics and Mathematics, Kathmandu: M.K publishers and Distributors.
- Batty, j.:(1963), Management Accounting, London: Macdonald and Evans.
- Brain, O, Ogley,(1981), Business Finance, and London: Long man Inc.
- Brigham, Eugene F; (n.d.), Fundamentals of Financial Management, 3rd Edition, and Chicago: the Dryden Press.
- CBS, HMG/FOM, (2003) Economic Survey, 2002, Kathmandu.
- CBS, HMG/NPC, (2002) , Statistical pocket Book Nepal , Kathmandu.
- CBS, HMG/NPC, (2003) Nepal in Figure 2002, Kathmandu.
- Chudson, w. A.; (1965). The pattern of Corporate Financial Structure, New York: National Bureau of Economic Research.
- Clifton, Krebs, Richard F. Watch; (1975), Financial Administration , Chicago: The Dryden Press.
- Frances D. Pitt ; (1980), The Foundation Of Financial Management, 1st Indian Edition: Arnold Heinemann.
- Gesternberg, C. W. ;(1962), Financial Organization and Management of Business, Bombay: Asia Publishing House.
- Iqbal, Mathur; (1979), Introduction of Financial Management, New York; Mac Millan Publishing Co.
- Jain, Premila; (1969) Financial Management, Jaipur: Pointer Publications.
- Johnson, R. L.; (1973), Financial Decision Making, Goodyear Publishing Co. Inc.
- Joshi, P. R.; (2001), Research Methodology, 1st edition, and Kathmandu: Buddha Academic Enterprises Pvt, Ltd.

- Khan, M. Y. ; Jain, P.K.:(1995), Financial Management, New Delhi: Tata McGraw Hill.
- Kothari, C. R.:(1990), Research Methodology: Methods and techniques, 2nd Edition, New Delli: Wishwa Prakashan.
- Kuchhal, S.C.; (1977), Financial Management: An Analytical and Conceptual Approach, Chaitanya publishing house.
- Kulkarni, P. V.:(1983), Financial Management, Bombay: Himalaya Publishing House.
- Lawrence D. Schell and Charles W. Haley; (1983). Introduction to Financial Management, 3rd edition, New Delhi: Tata Mc Graw Hill.
- Mc Grath Michael. (1949), financial intuition, instrument and markets 3rd Edition.
- Mummy, A. Glen ;(1969), Theory of financial structure, Hall, Reinhart and Wiston Inc.
- Nepal Stock Exchange Ltd; (1994), Financial Statement of listed Companies, Vol. IV, Kathamndu.
- Nepal Stock Exchange Ltd; (1997), Financial Statement of listed Companies, Vol. IV, Kathamndu.
- Pandey, I. M.; (1985), Financial Management, 7th Revised edition, New Delhi: Vikas Publishing House Pvt, Ltd.
- Pandey, I. M.; (1995), Financial Management, 7th Revised edition, New Delhi: Vikas Publishing House Pvt, Ltd.
- Phillipatos, George C.:(1974), Essential of Financial Management Text and Cases, Holden Day Len.
- Prsanna, Chandra; (n.d), Fundamental of Financial Theory and Practice , 5th Edition, New Delhi : Tata McGraw Hill.
- Prsanna, Chandra; (n.d), Fundamental of Financial Theory and Practice, 2th Edition, New Delhi : Tata McGraw Hill.
- Shrivastav, R. M.; (1984), Financial Management.

Solo man, Ezra; (1963), Theory of Financial Management, and New York: Columbia University Press.

Solo man, Ezra; (1996), Theory of Financial Management, and New York: Columbia University Press.

Steven E Bolten “Essential of management fiancé.”

Sylvan D. Schwartz man and Richard E. Bill; (1977), Elements of Financial Statement Analysis, New York: Van No trend company.

Upadhaya, K.M. ; 1985, financial management, Kalyani Publishing India.

Van Home, James C.:(1994.), Fundamental of Financial management and policy,, 4rd edition , New Delhi: Prentice Hall of India P. Ltd.

Van Home, James C.:(n.d.), Fundamental of Financial management, 3rd edition, New Delhi: Prentice Hall of India P. Ltd.

Walker Ernest, W.:(1976), Financial Management, 2nd Edition, New Delhi: Prentice Hall of India P. Ltd.

Weston J Fred; Brigham, Eugene F.:(1978), Management Finance, 6th edition, Chicago: The Dryden Press.

Wolff, Howard K. and Pant. Prem R; (1999), Social Science Research and Thesis Writing, 2nd Edition, and Kathmandu: Sewa Printing Press Center.

Thesis:

Aryal, Ramesh R.:(1991), An Evaluation of Capital Structure of Bothers Nepal Ltd, An Unpublished, MBA, T.U.

Dahal, Bhanu Nath; A study of financial ratio as Indicators of Profitability, An Unpublished Dissertation; MBA, T.U.

G.C., Bal Krishna;(1998), A study on Capital and Assets Structure of Rastriya Beema Sansthan , An Unpublished Dissertation, MBA, T.U.

Prashai, Shanti Raj: (1999), Capital Structure & Profitability: A Comparative Case study Between Nepal Indoseuz Bank Ltd. and Nepal Grind lays Bank, An Unpublished Dissertation; MBA, T.U.

Parajuli, Sambhu Parshad(2001); Capital Structure and its Impact on profitability of Nepal lever Ltd. An Unpublished Dissertation; MBA, T.U.

Panta, Youba; A study of Capital Structure of NIDC, An Unpublished Dissertation; MBA, T.U.

Rajlawat, Kaml Bahadur; (1999), Capital Structure of Necon Air Ltd., An Unpublished Dissertation; MBA, T.U.

Tamang, G.B.; (2001), An impact of Capital Structure on Profitability, An Unpublished Dissertation; MBA, T.U.

Website

www.Nepalstock.com

Dear Sir/Madame,

I would like to introduce myself as a student of Master of Business Studies (MBS) in Tribhuvan University, Shanker Dev Campus, Putalisadak, Kathmandu. In order to fulfill the partial requirements of Master's Degree in Management, I am conducting a research work entitled "**Capital Structure Management of Selected Manufacturing Companies in Nepal**". I would very much appreciate if you kindly spare few of your busy and valuable time for completing my research work. Your views are purely used for my academic purpose only. I anticipate your suggestions as soon as possible.

Sincerely yours,

Mahesh Sharma

Shanker Dev Campus

Questionnaire

- 1) What did you understand by the word 'Capital Structure'?
 - a) Equity Capital
 - b) Debt Capital
 - c) Equity and Debt Capital
- 2) Who takes the decision on capital structure of a firm?
 - a) Shareholders
 - b) Board of Directors
 - c) Chief Executive Officer
- 3) Which one is riskier capital in capital structure?
 - a) Equity Share Capital
 - b) Debt Capital
 - c) Equity and Debt Capital

- 4) Which capital is preferred in Inflation rate in double figure?
- a) Equity Share Capital
 - b) Debt Capital
 - c) Equity and Debt Capital
- 5) In current scenario, which type of problem facing by Nepalese Manufacturing companies?
- a) Capital Problem
 - b) Raw Material problem
 - c) Security problem
 - d) Trained Manpower problem
- 6) In Nepal, which type of policy existing in Manufacturing Companies?
- a) Liberal Policy
 - b) Political Influence
 - c) Influence by other developing nations policy
- 7) Profit sharing in dividend and retained earning policy
- A) Dividend distribution – high percentage
 - B) Retained Earning - High percentage