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A STUDY ON CAPITAL STRUCTURE AND FINANCIAL LEVERAGE WITH REFERENCE TO RELIANCE INDUSTRIES

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Abstract:

Capital structure refers to the mix of long term sources of funds, such as debentures, long-term debt, preference share capital and equity share including reserves and surplus. Some companies don't plan their taken by the finance manager without formal planning. These companies may prosper in the short run, but ultimately they may face considerable difficulties in raising funds to their activities the financial manager should plan an optimum capital structure for his company. The optimum capital structure is obtained when the market value share is maximum. The main objective of the study is that to analyse the financial position of the company through various factors. For this purpose a sample of 5 years was taken in to consideration were ratio analysis was used as tools to analyse the data. The conclusion is that the long term financial position of the company was good and satisfactory mean while the short term financial position was not up to the standards and the company has to look after the short term financial position to maintain a stable financial position in future.

Key Words: Funds, Capital Structure & Financial Position

Introduction:

Capital structure refers to the composition or make up of long term sources of funds such as equity shares, preference shares, debentures and long term loans. The essence of capital structure problem is to decide the ratio of debt capital to equity capital. Capital structure decision is one of the important decision the chief financial officer of company should take. It should develop an appropriate or target capital structure which is most advantageous to the company. This can be done only when all those factors which are relevant to the company's capital structure decisions are properly analysed and balanced. The optimum capital structure is one that maximizes the market value of the firm. The capital structure may vary among industries and among companies within an industry. Since a number of factors influence the capital structure decision of a company the judgment of the person making the capital structure decision plays a crucial part. These factors are highly psychological, complex and qualitative.

Scope of the Study:

The study attempts to analyze the capital structure and financial leverage of Reliance Industries .various ratios related to capital structure is calculated and analyzed to study the efficiency of the organisation in dividing its proportion of long term capital. Financial leverage is analyzed to see how effective the organisation has tries to achieve the wealth maximization objectives. From the above analysis and findings, researcher has attempted to give use full suggestions to improve the capital structure and financial leverage of Reliance industries.

Objectives of the Study:

- ✓ To analyze the capital structure of the company.
- ✓ To analyze profitability of the company.
- ✓ To analyze the debt and equity position
- ✓ To know the financial leverage of the company.

Research Methodology:

Research Design: The present study aims at analyzing the capital structure and financial leverage at Relianc E Industries.

Period of the Study: The period of study covers five years 2013-2014 to 2017-2018.The data collected from the published annual reports of the selected company for 5 years period have been suitably re-arranged, classified and tabulated as per requirements of the study.

Source of the Data: The study is mainly based on secondary data, which has been collected from the annual report of Reliance industries.

Tools Used for the Study: The tools used for the study were accounting tool.

Accounting Tool:

- ✓ **Ratio Analysis:** In financial analysis, a ratio is used as a benchmark for evaluating the financial position and performance of firm.

Limitations of the Study:

- ✓ The study is based on secondary data viz, published annual report of the companies. The reliability and accuracy of calculations depend very much on the information. Found in the balance sheet.
- ✓ The study period is for 5 years 2014-2018.

- ✓ The figures taken for the calculations are most approximate.
- ✓ The time limit for conducting the study is very short.

Analysis and Interpretation:

Debt Equity Ratio:

Year	Outsiders Fund	Shareholders Fund	Debt Equity Ratio
2012-2013	48034	166096	0.29
2013-2014	43012	180020	0.24
2014-2015	62708	197091	0.32
2016-2017	76227	216176	0.35
2017-2018	76766	240184	0.32

The debt-equity ratio for the year 13-14 shows 0.29 & 14-15-0.24 & 15-16-0.32 & 16-17-0.35 & 17-18-0.32. Hence its shows a fluctuating trend. The low debt equity ratio is considered a favorable from the long-term creditors point of view. A high debt equity ratio indicates that the claims of outsides are greater than owner is not considered by creditor because of lesser margin of safety.

Proprietary or Equity Ratio:

Year	Shareholders Fund	Total Asset	Ratio
2012-2013	166096	295140	0.56
2013-2014	180020	318511	0.57
2014-2015	197091	367583	0.54
2016-2017	216176	397785	0.54
2017-2018	240184	457720	0.52

The proprietary ratio or equity ratio for the year 12-13-0.56 and 16-17-0.54 and 17-18-0.52. Hence its shows a fluctuating trend. A higher the ratio better is the long-term solvency position of the company.

Fixed Assets to Net Worth:

Year	Fixed Assets	Shareholders Fund	Ratio
2012-2013	113723	166096	0.68
2013-2014	109748	180020	0.61
2014-2015	109406	197091	0.56
2016-2017	114563	216176	0.53
2017-2018	131410	240184	0.55

The fixed assets net worth ratio during the study period ratio showed higher in 2011-12-0.68 and lower in 2015-16-0.53. This ratio 60-65 percent is considered to be satisfactory ratio in case of industrial undertakings.

Ratio of Current Assets to Proprietors Funds:

Year	Current Assets	Shareholders Fund	Ratio
2012-2013	132344	166096	1.78
2013-2014	143976	180020	1.77
2014-2015	135333	197091	1.87
2016-2017	116152	216176	1.84
2017-2018	90564	240184	1.91

The above table shows ratio of current asset to proprietor fund. During the study period ratio showed higher in 2016-17-1.91 and lower in the 2013-14-1.77. This ratio indicates the extent to which proprietors funds are invested in current assets.

Interest Coverage Ratio:

Year	Net Profit	Fixed Interest	Ratio
2012-2013	33649	2667	12.6
2013-2014	30714	3036	10.1
2014-2015	30766	3206	9.6
2016-2017	31602	2367	13.4
2017-2018	40139	2454	16.2

The above table shows interest coverage ratio. During the study period ratio showed higher in 2016-17-16.2 and lower in the year 14-15-9.6. It shows a fluctuating trend. Higher the ratio more safe are the long-term creditors.

Return on Shareholder Investment:

Year	Net Profit	Shareholders Fund	Ratio
2012-2013	20040	166096	0.12
2013-2014	21003	180020	0.12
2014-2015	21984	197091	0.11
2016-2017	22719	216176	0.11

2017-2018	27417	240184	0.11

The Return on shareholders' investment, shows a decreasing trend. During the study period the company showed a higher ratio of 0.12 in the year 2011-2013.and the lower ratio of 0.11 in the year 2014-2016. Lower ratio shows lower return on investment

Earnings per Share:

Year	Net Profit	No of Equity Share	Ratio
2012-2013	20040	29787.05	0.67
2013-2014	21003	29363.09	0.71
2014-2015	21984	29395.47	0.74
2016-2017	22719	29433.34	0.77
2017-2018	27417	29480.22	0.93

The earning per share of the company shows a increasing trend. During the study the company showed a higher ratio of 0.93 in the year 2017-2018. And lower ratio of the year 2012-2013.the earning per share is a good measure of profitability.

Return on Net Capital Employed:

Year	Net Profit	Net Capital Employed	Ratio
2012-2013	20040	226252	0.09
2013-2014	21003	235225	0.089
2014-2015	21984	272017	0.080
2016-2017	22719	306484	0.074
2017-2018	27417	332698	0.082

The return on net capital employed shows a fluctuating trend. During the study period the company showed a higher ratio of 0.089 in the year 2013-2014.and the lower ratio of 0.09 in the year 2012-2013.it shows the total asset used in a business less its current liabilities.

Capital Turnover Ratio:

Year	Sales	Net Capital Employed	Ratio
2012-2013	329904	226252	1.46
2013-2014	360297	235225	1.52
2014-2015	390117	272017	1.43
2016-2017	329076	306484	1.07
2017-2018	233158	332698	0.70

The capital turnover ratio shows a fluctuating trend and decreasing trend. During the study period a company showed a higher ratio of 1.52 in the year 2012-2013.and lower ratio of 0.70 in the year 2017-2018.it is used to measure the efficiency which a firm utilizes its resources. This ratio is a good indicator of overall profitable of the concern.

Fixed Assets Turnover Ratio:

Year	Sales	Fixed Assets	Ratio
2012-2013	329904	113723	2.90
2013-2014	360297	109748	3.28
2014-2015	390117	109406	3.56
2016-2017	329076	114563	2.87
2017-2018	233158	131410	1.77

The fixed asset turnover ratio shows a shows a fluctuating trend. During the study period the company showed a higher ratio of 3.56 in the year 2014-2015.and the lower ratio of 1.77 in the year 2017-2018.it shows the relationship between the cost of goods sold and fixed asset employed in a business.

Total Investment to Long-Term Liabilities:

Year	Shareholders Fund & Long Term Liabilities	Long Term Liabilities	Ratio
2012-2013	226252	60156	3.76
2013-2014	235225	55205	4.26
2014-2015	272017	74926	3.63
2016-2017	306484	90308	3.40
2017-2018	332698	92514	3.60

The total investment to long term liabilities shows a fluctuating trend. During the study period the company showed a higher ratio of 4.26 in the year 2013-2014.and the lower ratio of 3.40 in the year 2016-2017.it help to find the capital structure of the company and its long term liabilities.

Ratio of Fixed Assets to Funded Debt:

Year	Fixed Assets	Funded Debt	Ratio
2012-2013	113723	48034	2.36

2013-2014	109748	43012	2.55
2014-2015	109406	62708	1.74
2016-2017	114563	76227	1.50
2017-2018	131410	76766	1.71

The fixed asset to funded debt shows a decreasing trend and fluctuating. During the study period the company showed a higher ratio of 2.55 in the year 2013-2014.and the lower ratio of 1.50 in the year 2016-2017.it shows a proper mix of debt and equity capital in financing the firms asset.

Ratio of Current Liabilities to Proprietors Fund:

Year	Current Liabilities	Shareholders Fund	Ratio
2012-2013	68888	166096	0.41
2013-2014	83286	180020	0.46
2014-2015	95566	197091	0.48
2016-2017	91301	216176	0.42
2017-2018	125022	240184	0.52

The current liabilities to properitors funds shows a increasing trend. During the study period the company showed a higher ratio of 0.52 in the year 2017-2018.and the lower ratio of 0.41 in the year2012-2013.

Financial Leverage:

Year	EBIT	EBT	Financial Leverage
2012-2013	33619	25750	1.30
2013-2014	30714	26284	1.16
2014-2015	30766	27818	1.10
2016-2017	31602	29468	1.07
2017-2018	40139	35701	1.12

The financial leverage shows a fluctuating trend. The company showed a higher ratio of 1.30 in the year 2012-2013 and lower ratio of 1.07 in the year 2016-2017. A lower ratio indicates a low rate of interest and consequently lower borrowings.

Ratio Analysis:

- ✓ The debt equity ratio was highest in the year 2016-2017 at 0.35 times and was lowest in the year 2014-2015 at 0.24 times. The lower ratio implies smaller claims from creditors because of low debt during the year.
- ✓ The proprietary ratio doesn't shows any difference over the years. The ratio was highest in the year 2013-2014 at 0.56 times and was lowest in the year 2017-2018 at 0.52 times. Thus, if the ratio is high the firm can be more concerned.
- ✓ The fixed assets net worth ratio was highest in the year 2013-2014 at 0.68 times and was lowest in the year 2016-2017 at 0.53 times.
- ✓ The current asset to proprietor fund was highest in 2017-2018 at 1.91 and was lowest in the 2014-15 at 1.77. This ratio indicates the extent to which proprietors funds are invested in current assets. There is no "rule of thumb" for this ratio.

Suggestions:

- ✓ The company has to look after the operations of the company to increase the current ratio to 2:1 in future to stabilize the financial position of the company.
- ✓ Though Current asset to proprietors fund ratio is increasing the company has to increase the current assets further so that the return towards proprietors fund can be increased.
- ✓ If the liquidity increases then there may an chance to increase in the debt equity ratio of the company.
- ✓ As the company's liquidity has a shortfall towards its standard ratio it is preferred to decrease the fixed assets to stabilize the short term financial position of the company.
- ✓ If the firm tries to look after short term profit of the firm then the operating profit ratio may increase further in near future.
- ✓ If the debt decrease then there a possibility of positive impact towards short term financial position of the firm.

Conclusion:

The conclusion is that the long term financial position of the company was good and satisfactory mean while the short term financial position was not up to the standards and the company has to look after the short term financial position to maintain a stable financial position in future.

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