PDF - THE IMPACT OF WORKING CAPITAL STRUCTURE ON GROWTH AND SUSTAINABILITY OF BUSINESS ENTITY ON CORPORATE PERFORMANCE IN NIGERIA - researchcub.info**ABSTRACT**

The study investigates the impact ofworking capital structure on growth and sustainability of business entity.Specifically, it assesses the relationship between profit after tax and debt,equity and retained earnings. A sample of ten selected quoted companies on the Nigeriastock exchange was used.

The study used the multiple regressionmodel to look at The impact of working capital structure on growth andsustainability of business entity on the profit after tax of the sampledcompanies spanning a period of ten years (2001 -2010).

The finding of the study showed that thereis a significant relationship between capital structure and corporateperformance of selected companies measured in terms of profit after tax. Theregression showed that retained earning showed more relationship with profitafter tax than equity and debt.

The study thus recommended that companiesshould make a proper appraisal of the various source of capital required forbetter performance and emphasized the importance of efficient management ofcapital structure of a firm.

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CHAPTERONE: INTRODUCTION

1.1 BACKGROUNDSTO THE STUDY

Capital structure remains one of thepopular topics among the scholars in finance field. It refers to the financialframework of a firm which comprises of debt and equity used to finance thefirm. Capital structure in financial term means a way a firm finances itsassets through the combination of equity, debt or hybrid security(Saad, 2010).

According to Pandey (1995), capitalstructure is define as the proportionate relationship between the variouslong-term forms of financing such as debenture, long- term debt, preferencecapital and common/ share capital including reserves and retained earnings.

The capital structure choice has long beenan issue of great debate in the corporate finance literature. For sometime now,there has been argument whether the way a firm is financed matters. That is,whether exist an optimum capital structure which a firm must adhere to in orderto achieve its objective of shares holder's wealth maximization. Another areaof argument is the probable effect of changes in a firm financing mix on itsmarket value and its cost of capital.

Determination of an appropriate capitalstructure for a firm is a critical decision. This is not as a result of theimportance of such decision to maximize return but because of the importance ofsuch decision to maximize return but because of the impact such decision has onthe firm ability to deal with its competitive environment. Capital structurecan be used to finance investment which is other wise refers to as financingdecision. This financing decision can affect the debt–equity mix of a firm andthis debt-equity mix has an overall implication on 9/the shareholders earningand corporate performance firms in Nigeria.

Generally, there are basic two source ofcapital. The internally generated source of capital and the externally generatedsource of capital (Oyejide, 1987). The internally generated source of capitalcomprises of mainly equity capital and retained earnings. These two forms ofcapital under internally sources of finance are referred to as theshareholder's funds.

The other source of finance is theexternally generated source of capital. This is loan capital or debt finance.Thus, investment projects of a capital can be financed either by increasing theowners claims or the creditors claims. The owners' claims increase when thefirm raises funds by issuing common shares or by retaining earnings; Thecreditors claims increase by borrowings.

The financing or capital structure decisionis a significant managerial decision as it influences the shareholders returnsand risks. Consequently, the market value of the firm is determined by thecapital structure decision. The company will have to plan its capital structureinitially at the end of its promotion and subsequently. Whenever, funds have tobe raised to finance investment projects, capital structure decision isinvolved.

Generally, the capital structure of a firmpresumed any of the following patterns (10% equity, 0% debt), 0% equity, 100%debt, (X% equity, Y% debt). Option one is that of unlevered firms where thefirm ignores advantages (if any) of leverage. Option two is quite unrealisticin real life situation as no investors would want to invest his money in a firmwithout equity capital.

This partially explains the term “trading on equity”.That is, it is the equity element that is present in the firm’s capitalstructure that encourage the debt provides to give their sources resources tothe business option three is the most realistic one in that it contained both acertain percentage of equity and debt in the capital structure and thus, theadvantage of leverage (if any) is exploited.

1.2 STATEMENT OF THE PROBLEM

Capital imposed different obligations andcosts on the firm. Managers when deciding on the optimal capital structure forthe firm, take into consideration the cost of capital and the risks.

The actual effects of capital structure oncorporate performance in Nigeriahas been a major problem among researchers that as not been resolved. Zeitumand Tian (2007) find out that capital structure has a significant and negativeeffect on the forms performance measure in both accounting and market measures.However, the proportion in which debt and equity are combined would influenceboth the firm’s value and the overall cost of capital (K_0). At thispoint, the management has to divide from the outset whether or nor to employdebt in its financing mix. If ‘yes’ what proportion of debt-equity willmaximize the total value of the firm or minimize the overall weighted averagecost of capital (WACC).

Moreover, the capital structure and corporateperformance in Nigeria whichsought to find the actual financing behaviour of firms in Nigeria and the factors thatinfluence the financing decision had not been stable overtime. However, a greatnumber of these empirical studies carried out in Nigeria have not been givenattention as it is in developed countries.

In light of the above, it was necessary toevaluate The impact of working capital structure on growth and sustainabilityof business entity or corporate performance in Nigeria.

1.3 OBJECTIVE OF THE STUDY

The broad objective of this research is toevaluate the impact of working capital structure on growth and sustainabilityof business entity on corporate performance in Nigeria. The specific are:

i. Todetermine whether the capital structure of a firm has effect on the corporateperformance or firm’s value.

ii. Todetermine the effect of leverage on the growth in earning of a firm.

iii. Toknow the particular proportionate combination of debt and equity that providesthe best expected trade off

iv. Totest the validities of capital structure theories on the experience of quotedcompanies in

Nigeria and thereby providing up-to date evidence to validate existingstudies and thereby serving as guiding post for the future conduct of capitalstructure in Nigeria.

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