A Study on Capital Structure and Long - Term Solvency Position of Tata Steel Limited

R. Sathish Kumar
MIET Arts & Science College, Gundur, Trichy, Tamilnadu

Abstract- *Capital Structure and Long-Term Solvency position is very important to every company which in profit making motive companies. According to this concept, the present study is made to assess the capital structure and long term solvency position of Tata Steel Company. The present study use the financial tools like percentage and ratios to analyze the data from 2000-01 to 2014-15. Based on results and findings the suggestion is given which is applicable only to Tata Steel (Stand-alone) Limited Only.*

Keywords- Long-Term, Capital Structure, Percentage, Ratios, Tata Steel Limited.

I. INTRODUCTION

Achievement of financial management objectives is very critical aims of finance manager. One of the main objectives of financial management is maximization of shareholders wealth, which means the firm should increase the value (equity shares) of the firm. Therefore, the firm selects the financing mix/ capital structure/ financial leverage, which is helps to achieve the financial management objective. In the context, capital structure plays an important role in the value of the firm. It is nothing but the combination of debt and equity of capital structure.

In case the firm used higher portion of debt while compare with equity then the firm high levered firm and also debt is cheapest source of fund and it create tax shields because the interest is detectable as a expenses from the taxable profits as well as it leads to financial distress or insolvency. On the other hand the firm used only equity shares only, then it is called unlevered firm while compare with debt finance it is costly and less risky but it could not enjoy the leverage facilities. Long-term solvency ratio, which is measure the firm’s soundness on the basis of long-term financial strength. It is also called Leverage ratio or Capital Structure ratios.

A. Review of Literature

Amalendu Bhunia and Islam Uddin Khan (2011) in their study analyzed the liquidity management efficiency and solvency position of Indian steel companies. Liquidity management is most important in financial management decision. The study analyzed the association between the liquidity management and profitability of 230 Indian private sector steel companies obtained from CMIE database. Liquidity management indicators and profitability indicator over the period from 2002 to 2010 is modeled as a linear regression system in multiple correlation and regression analysis. A descriptive statistics discloses that liquidity and solvency positions are highly satisfied. Multiple regression tests confirmed a lower degree of association between the liquidity management and profitability.

S. Kandasamy and M. P. Mahesh (2011) in their article analyzed the financial health of SAIL through Z score analysis. The Z score analysis is used to predict the corporate difficulties. The Z score model incorporates five weighted financial ratios such as the ratio of working capital to total assets, the ratio of retained earnings to total assets, EBIT to total assets, market value of equity to total debt and net sales to net assets. The profitability affected due to increase in all major elements of the Z-score. The cost component of the company increased but low overall borrowing strengthen the company to mobilize the recourses while keeping the leverage at managing level so it concludes that, the financial health shown by Z score analysis during that period reveals better management of the solvency position of the company.

Asha Sharma (2012) in her study analyzed the capital structure of Tata steel limited. Steel Industry in India is on an upswing because of the strong global and domestic demand. India's rapid economic growth and soaring demand in sectors like infrastructure, real estate and automobiles, at home and abroad, has put Indian steel industry on the global map. This paper has analyzed capital structure, financial leverage, earnings per share and dividend per share of steel industry for the period of 2006 to 2010. Statistical results revealed that there is a correlation between Degree of Financial Leverage and Earnings per Share & Degree of Financial Leverage and Dividend per Share & Earnings per Share and Dividend per Share.

B. Statement of the Problem

The Indian Steel industry need large investment and suffers from paucity of capital. Many of the public sector undertaking units integrated steel plants with the help of foreign aid. Lack of modern technological and capital inputs and weak infrastructural facilities leads to a process of steel making that is more time consuming, expensive and yields inferior variety of goods. Such a situation forces to import better quality steel from abroad.

Tata Steel is one of the best steel industries and occupies 11th position among the steel companies in the world, having subsidiaries and joint ventures throughout the world. In this context, the present study has taken Tata Steel Limited as a study unit to study the capital structure.

C. Objective of the Study

The following are the main objective of the present study.

1) To estimate the capital structure pattern of the Tata Steel Limited (Stand-alone)
2) To assess the long-term solvency position of the company

D. Methodology

The study used only the secondary data to attain the objectives of the study. The data take from the annual report of the company, which is available in the company website and capital line database. This study has confined to Tata Steel Limited (Stand-alone) only. Subsidiary companies of Tata Steel have been excluded from the present study. To estimate the capital structure pattern and long-term solvency were Simply Percentage Analysis and Ratios are used in the present study.

The study covers 15 financial years from 2000-01 to 2014-15 to make the analysis of capital structure and long-term solvency that are deemed quiet sufficient.

E. Limitation and Area of further Study

Reliability of results of the study has purely based on the reliability of the secondary data. The study has not covered subsidiary and foreign companies of the Tata Steel Limited. The study does not cover any non-financial data. The further study may conduct through by analyzing the short-term solvency and liquidity position of Tata steel limited by stand-alone or considering the overall performance.

II. ANALYSIS AND INTERPRETATION

Table – 1: Common Size Capital Structure Statement of Tata Steel Limited

Particulars	Equity Share Capital	Share Application Money	Preference Share Capital	Reserves	Borrowed Fund	Total Long Term Funds
2000-01	3.85	-	1.46	45.82	48.87	100.00
2001-02	4.51	-	-	37.75	57.74	100.00
2002-03	4.96	0.02	-	38.01	57.01	100.00
2003-04	4.68	-	-	52.56	42.76	100.00
2004-05	5.65	-	-	66.39	27.96	100.00
2005-06	4.51	-	-	74.98	20.50	100.00
2006-07	2.45	0.62	-	56.31	40.63	100.00
2007-08	1.61	-	12.07	46.55	39.76	100.00
2008-09	1.29	-	9.66	41.48	47.57	100.00
2009-10	1.42	-	-	58.14	40.44	100.00
2010-11	1.31	0.24	-	62.67	35.77	100.00
2011-12	1.27	-	-	67.68	31.05	100.00
2012-13	1.20	-	-	66.86	31.94	100.00
2013-14	1.11	-	-	68.95	29.94	100.00
2014-15	1.05	-	-	70.73	28.22	100.00

Source: Computed from Secondary data, Annual Report of TSL.

Note: figures in Percentage.

It is observed that from the above table that Equity share capital to total capital structure position of the company fluctuating in nature. The maximum proportion of Equity share capital with capital structure is 5.65 percent in 2004-05 and minimum of 1.05 percent in 2014-15. First three years of the study period, the Equity share proportion shows increasing trend from 3.85 per cent to 4.96 per cent. Except 2004-05 and 2009-10 rest years shows decrease in trend. The company has meager amount of share application money in the capital structure 2002-03, 2006-07 and 2010-11 as a per cent of 0.02, 0.62, and 0.24 respectively. The company held convertible perforce share capital of 1.46 per cent in 2000-01, 12.07 per cent in 2007-08 and 9.66 percent in 2008-09.

The growth of reserve and surplus of the company shows two stages an increasing trend in 2001-02 to 2005-06 and 2008-09 to 2014-15. It ranges from 37.75 percent in 2001-02 to 74.98 percent in 2005-06. The highest percent of reserve and surplus recorded in the year 2005-06. During the study period, the borrowed fund portion to capital structure shows fluctuating trend and it ranges from 28.22 percent in 2014-15 to 57.74 percent in 2001-02.

Table – 2 : Coverage Ratio of Tata Steel (Stand-alone) Limited

Particulars	Coverage Ratio			
	Interest	Dividend (Preference Dividend)	Dividend (Equity Dividend)	Total Cash flow Coverage
2000-01	2.60	-	2.54	3.91
2001-02	1.68	98.99	1.39	3.08
2002-03	5.14	-	3.04	6.96
2003-04	22.82	-	4.20	27.94
2004-05	29.36	-	4.23	32.67
2005-06	45.24	-	4.27	51.79
2006-07	37.01	-	3.82	41.72
2007-08	9.04	211.22	3.42	9.75
2008-09	7.35	47.53	3.76	7.48
2009-10	5.78	110.00	6.06	6.31
2010-11	8.52	-	5.25	9.40
2011-12	6.12	-	4.97	6.72
2012-13	5.18	-	5.59	6.05
2013-14	6.34	-	6.18	7.39
2014-15	5.31	-	6.92	6.32

Source: Computed from Secondary Data, Annual Report of Tata Steel Limited

The interest coverage ratio shows fluctuating trend over the study period. The highest interest cover in profit is 45.24 times in 2005-06 and lowest 1.68 times in 2001-02. The preference dividend coverage ratio of the company has recorded in the year 2001-02, 2007-08, 2008-09 and 2009-10 as 98.99, 211.22, 47.53 and 110 times to profit. The equity dividend coverage ratio shows highest times in 2014-15 as 6.92 times and lowest 1.39 times in 2001-02. The total cash flow coverage ratio ranges from 3.08 times in 2001-02 to 51.79 times in 2005-06.

Table – 3

Long-term Solvency Ratios of Tata Steel Limited

Particulars	Debt-Equity Ratios				Proprietary Ratio
	External equities to internal equities	Debt to total long-term funds	Shareholders fund to total long term funds	Total long term funds to shareholders fund	(Shareholders fund/Total tangible assets)
2000-01	1.56	0.49	0.51	1.96	0.42
2001-02	2.71	0.58	0.42	2.37	0.29
2002-03	3.15	0.57	0.43	2.33	0.24
2003-04	2.35	0.43	0.57	1.75	0.30
2004-05	1.36	0.28	0.72	1.39	0.43
2005-06	0.97	0.21	0.79	1.26	0.52
2006-07	1.27	0.41	0.59	1.68	0.44
2007-08	1.02	0.40	0.60	1.66	0.50
2008-09	1.31	0.48	0.52	1.91	0.43
2009-10	1.00	0.40	0.60	1.68	0.50
2010-11	0.91	0.36	0.64	1.56	0.52
2011-12	0.83	0.31	0.69	1.45	0.55
2012-13	0.85	0.32	0.68	1.47	0.54
2013-14	0.82	0.30	0.70	1.43	0.55
2014-15	0.74	0.28	0.72	1.39	0.58

Source: Computed from Secondary data, Annual Report of TSL.

The debt: equity ratio can measure by various aspects. The measurement in the aspect of external equities to internal equities, the ratio shows the company pays it external liabilities from its available internal equities. The internal equities consist of share capitals, outsider liabilities of the company consist borrowings of short-term as well as long-term. While considering this aspect ratio, the company implied low safety margins in the years 2000-01, 2001-02, 2002-03, 2003-04, 2004-05, 2006-07 and 2008-09 because the company pays the outsider liabilities more than the internal equities as times of 1.56, 2.71, 3.15, 2.35, 1.27 and 1.31 times respectively. During the study period the company external equities to internal equities ratio shows fluctuating in nature due to more external equities in nature. From 2009-10 onwards the company has controlled the ratios through increase the internal equity strengthen so the company has high safety of margin. It is surprising to noted that the equities of internal as well as external is more or less same proportion in the years 2005-06, 2007-08 and 2009-10 as 0.97, 1.02 and 1.00 times respectively.

The consideration of total debt to total long-term fund ratio is showing a decreasing trend. The maximum recorded in the year 2001-02 as 0.58 times and minimum of 0.28 times of debt to total long-term capital in the year 2004-05 and 2014-15. Shareholders fund to total long-term fund shows an increasing trend the maximum proportion recorded 0.72 in the year 2004-05 and 2014-15. The proportion of debt to long-term funds and equity to long-term funds shows a negative correlation. It is interesting to note down that the debt: equity proportion 0.28:0.72 (3:9) shows to total long term funds in the years 2004-05 and 2014-15, it is happened after ten years of the period.

The ratio for debt to total long-term fund and shareholders' funds to total long term funds may taken as ideal if the ratio are 0.5 which means the investors point of view may take debt-equity ratio is quite satisfactory if the shareholders funds are equal to borrowed funds. The low ratio indicates says above 0.5(>0.5) borrowed funds and less than 0.5(<0.5) owned funds, may also not be considered as unsatisfactory if the business needs heavy investment on fixed assets and has return on investment. In the point of view the investors satisfactory in the years 2000-01, 2001-02, 2002-03 and 2008-09 the rest years shareholders are satisfactory and vice versa.

The total long-term funds to shareholders funds show a fluctuating trend and 2008-09 onwards, the proportion shows a decrease in trend. The maximum proportion recorded 2.37 percent in the year 2001-02. The proportion is ideal when it is one so all the years the ratios shows an ideal one.

The proprietary ratio is no constant growth or decline in the ratio, it shows fluctuating trend in nature. The maximum ratio shows in the year 2014-15 as 0.58. The high proprietary ratio indicated that the company has well. There company should strengthen the proprietary ratio.

III. INDINGS SUGGESTIONS AND CONCLUSION

A. Relation to Capital Structure of the company

It is found that there is an opposite relationship between Reserves and Debt capital of the company. Therefore, it is suggested that there is no use of maintaining a high level of reserves and surplus amounts. It may be idle fund to the company. So insist of holding excess reserve and surplus f the company invests it to any other liquid form of assets it will help to generated more income and it can be utilize at emergency period. It will leads to efficient utilization of idle fund and the company may reduce to borrow the capital from the outsiders. So the company has limited liability to pay interest on borrowed capital and it can be help to improve the profit of the company and it will leads to high earnings per share so the company share price will also increase.

B. Relation to Long-term Solvency of the Company

The consideration of External and Internal equities ratio alone the company has not much safety in some years of the study period. Reaming year's company recovers from the low safety margin to high safety margin even though some years it showed equal level of external as well as internal equities. The recover option of the company is not fair, because it increase the reserves and surplus proportion of its capital structure because it may short-term sources of fund in some extent So the company can increase the equity share capital values instated of increase the reserve portion.

The overall debt and equity mix is well but the mix is not correlated with the company earnings per share. Therefore, it suggested that the company could use debt-equity mix as 1:1 it will satisfactory to both investors as well as shareholders of the company.

The proprietary ratio is importance to creditors. If the ratio is high will strengthen the shareholders but high ratio will indicate a relatively little danger to the creditors in the event of forced organization or winding up of the company. A low proprietary ratio indicates that greater risk to the creditors since in the event of losses a part of their money. Therefore, it is suggested that the company should maintain a moderate level of proprietary ratio to safeguard the company and maintain the name and fame of it.

The coverage ratios show a good performance in the years 2003-04 to 2006-07. The remaining years the company has shows a normal coverage on earnings. If the company concentrates on earnings; it will show the better recover ratios as shown in the previous financial year performance.

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