

REVIEW OF CORPORATE INVESTMENT IN SERVICE SECTOR IN INDIA

Naresh Vashist, Puneet Jain*

*Department of Management, CMJ University, Shillong Meghalaya,
India 793003.*

ABSTRACT

This paper shows about the finance practices in the corporate finance. There are three leading areas of corporate finance practices that consistently require the academic concentration of scholars in corporate finance theory. These include corporate financial practices relating to investing, financing and finally the practices concerning distribution. Corporate Finance has been the subject matter of coherent connotations among the researcher, corporate managers and the practitioners, ever since the evolution of corporate finance theory. Distinguished scholars, who visited the theory of capital budgeting, capital structure, cost of capital, capitalization, dividend policy and working capital of the firm, have come out with a number of recommendations that are of paramount understanding to budding researchers.

Keywords: *Corporate finance, coherent connotations, capitalization, dividend policy.*

OBJECTIVES AND METHODOLOGY

The objective of the study is to provide the awareness about the corporate investment in service sector in India. Here in this section, an attempt has been made to design and define a brief methodology commonly used to carry out the research work. The study is descriptive in nature and based on the secondary data that is gathered from the books, various articles from journals and other valid online sources.

REVIEW OF LITERATURE

In this paper, a brief review of researches, in the field of corporate financial practices, has been presented. The studies have been reviewed in the descending – cum – sequential order.

GROPP AND HEIDER (2008) are unable to detect a first order effect of capital regulation on the capital structure of banks and confirm the robustness of current corporate finance findings in a holdout sample of banks. Study documented that standard cross-sectional determinants of firm leverage also apply to the capital of large banks in the United States and Europe. It found a remarkable consistency in sign, significance and economic magnitude. Like non – financial firms, banks appears to have stable capital structures at levels that are specific to each individual bank.

RAABALLE AND JAKOB (2008) found that the characteristics of dividend payers are: Positive earnings, high ROE (net earnings to book equity), low volatility in ROE, high retained earnings, large firm size, and whether the firm paid out dividends in the previous year. MV/BV, leverage and owner structure play no role in whether a firm pays dividends or not. Among the dividend payers the generosity of the payments (relative to market value of equity measured in fixed prices) is positively related to ROE and previous year's generosity with respect to dividend payments and negatively related to concentrated owner structure and firm size. That is, the payer characteristics differ from the generous payer characteristics.

ANAND AND MALHOTRA (2007) developed quantitative benchmarks at the firm and the industry level to evaluate the working capital management performance of Corporate India. The study employed the methodology developed by Anand and Gupta (2003) and provides estimate by using the data of 339 S&P CNX 500 non-financial companies with at least three years of publicly available records over the period of study, Corporate India has achieved a Compound Annual Growth Rate (CAGR) of 26.3% in net sales and 1.6% in the operating cycle and cash conversion cycle has reduced by 10.2% and 12.7% respectively on compounded annual basis. The paper found very little evidence on the positive relationship between working capital management and firm profitability.

JOOS AND ZHDANOV (2007) examine, how the price – earnings relation varies with the uncertainty about and the quality of a firm's investment. The study developed a real option valuation framework to capture optimal investment and abandonment option in a research-intensive emerging technology, the biotechnology industry.

KANNADHASAN (2007) pointed out that many organizations that are profitable on paper are forced to cease their operations due to an inability to meet their short-term debt obligations. Ineffective management of working capital is one of the important factors causing industrial sickness. The study, by using the data available in the annual report for the period from 1998-99 to 2004-05, examined the working capital management of Titan Industries Limited. The study concluded that the liquidity position of this company is good and managed effectively.

REDDY G. AND REDDY S. (2007) established that working capital management assumes greater significance in Small Scale Industrial (SSI) Units as most of these have weak financial base and limited accessibility to financial markets. The present study attempts to study the working capital management practices in nine small scale industries located in Bangalore. The study covers units across industries as Automobiles, Batteries, Chemicals, Electrical, Engineering, Mineral, Plastic, Rubber and Steel. It was found that shortage of working capital is a chronic phenomenon with as many as 51 (cash) percent of the sample firms affirming this problem. Surprisingly, nearly 15 % of them do not face the problem at all. With regard to inventory shortage 38 % of the units never faced such problem.

TRUONG, PEAT AND GRAHAM (2007) used a sample survey to analyze the capital budgeting practices of Australian listed companies and found that NPV, IRR and Payback are the most popular evaluation techniques. Real options techniques have gained a toehold in capital budgeting but are not yet part of the mainstream. Discounting is typically by the weighted average cost of capital, assumed constant for the life of the project and with the same discount rate across divisions.

BAUER AND BHATTACHARYYA (2006) established that empirical modeling of dividends has been dominated by Lintner (1956). However, Lintner's model suffers from the logical paradox that if companies have target payout ratios then in the steady state the companies have reached those target payout ratios. The study established that Lintner's model is also poorly specified when earnings are serially correlated. The data have been tested by cross sectional Tobit regression as well as by time series models. The results of the Tobit regression are consistent with the predictions of their model. In time series testing, model fits the empirical reality at least 75% of the time. Moreover, for firms with longer data series of 35 years or more, it described the empirical data succinctly in 96% of the cases.

CHARISTOFFERSEN, JACOBS AND VAINBERG (2006) affirmed that few issues are more important for finance practice than the computation of market betas. Existing approaches compute market betas using historical data. The study used information embedded in the prices of individual stock options and index options to compute forward-looking market betas at the daily frequency. The model was implemented using option contracts for the thirty components of the Dow Jones index as well as data on S&P 500 options over the period 1996-2003. It was concluded that these forward – looking betas contain information relevant for forecasting future betas that is not contained in historical betas.

HAIL AND LEUZ (2006) examined international differences in firms' cost of equity capital across 40 countries. The final sample consists of 35,118 firm-year observations from 40 countries between 1992 and 2001. Results document substantial variation in the cost of equity capital across countries, much of which is explained by traditional proxies for risk, i.e. size, volatility and the book-to-market ratio, as well as country controls capturing international differences in inflation and macroeconomic variability. Together, these variables explain about 60% of the country-level and close to 40% of the firm-level variation in the implied cost of equity capital around the world.

JAIN AND KUMAR (2006) studied working capital management practices of Nifty index companies for the period 1991-2004. Statistical tools like correlation, regression and paired t-test were applied. It was concluded that sample nifty companies were opting for lower liquidity ratio for the period under study. Moreover, there is a declining trend in current ratio. However, the companies are managing their inventory more efficiently. Also, it has been found that more than 66% of the current assets are financed through current liabilities, the major share being from creditors and provisions.

PANDEY AND CHOTIGEAT (2006) examine the financial characteristics of Malaysian companies and their debt policies using data of 106 firms from 1992 to 1999. The results of pooled GLS regressions show that all types of debt (short-term, long-term and total) influenced by the variable for profitability, size and tangibility; but not by growth, risk and investment opportunity (market to book value ratio). Thus, the latter results are contrary to evidence from developed markets. In addition, the study found that when the data are classified into two sub-periods, only in the first (1992-1995) does the risk variable reveal the hypothesized positive influence on all debt ratios, reflecting Malaysia's economic uncertainty in the throes of the Asian financial crisis and implementation during the second sub-period (1996-1999) of the domestic capital control policy. It was concluded that profitability has a persistent negative relationship with all types of debt ratios in both periods; this confirms the capital structure.

BARCLAY AND SMITH (2005) presented review of available empirical evidence to assess the relative explanatory power of capital structure and dividend theories. The study attempted to determine the extent to which corporate leverage and dividend choices could be explained by differences in companies' investment opportunities. A cross-sectional regression technique was used, in which separate regression were run and coefficients were calculated for 54 years. The results provide strong support for the contracting cost hypothesis.

BHATTACHARYA, S K AND RAGHAVACAHARI, M (2005) attempt to identify a method of classifying those companies which manage their working capital more efficiently than others and to determine the factors which lead to the effectiveness of working capital management process. The discriminator analysis showed that the prime determinants of effectiveness of the working capital management, in order of relative importance, were: 1 Profit after Tax as a percentage of sales. Sales as number of times of total assets, quick assets as a percentage of current liabilities and receivables as number of days sales. The study recommended that the financial managers in the companies and the analysts in the financial institutions and commercial banks should pay more formal and explicit attention to these factors in their financial analysis.

BUFERNA, BANGASSA AND HODGKINSON (2005) provide further evidence of the capital structure theories pertaining to a developing country and examine the impact of the lack of a secondary capital market by analyzing these with reference to the Libyan business environment. The results of cross-sectional OLS regression show that both the static trade-off theory and the agency cost theory are pertinent theories to the Libyan companies' capital structure whereas, there are little evidence to support the asymmetric information theory.

MIAO (2005) present a competitive equilibrium model of capital structure and industry dynamics. In the model, firms make financing, investment, entry and exit decisions subject to idiosyncratic technology shocks. The capital structure choice reflects the tradeoff between the tax benefits of debt and the associated bankruptcy and agency costs.

ENY (2005) studied working capital management from the perspective of net – investment, having observed that present approaches do not take the question of operational size and relative liquidity of the firm into account when dealing with the issue of working capital adequacy. The research studied financial report of 25 selected listed companies together with opinion surveys on (existing) practical applications on working capital management in some of them. The results from data analysis were validated using a students' distribution test. The findings revealed that firms that considered relative liquidity performs better and have better growth prospect than other, while the study recommends the use of relative liquidity (relative solvency) for a more accurate estimation of working capital adequacy by organizations.

HABIB (2005) presented the brief review of empirical research on the relationship between information risk and the cost of capital. The study establishes that the finance theory suggests that, increase in information should reduce the cost of capital through reduced transaction cost and/or reduced estimation risk, traditional asset pricing model does not allow any role for information. This research documents recent development in the measurement of cost of equity capital and how this is affected by the quality of information disclosed.

HERMES, SMID AND YAO (2005) compared the use of capital budgeting techniques of Dutch and Chinese firms, using data obtained from a survey among 250 Dutch and 300 Chinese companies in the period between October 2003 and June 2004. Dutch CFOs use the NPV method significantly more often than their Chinese colleagues do. Second, Chinese CFOs use the ARR method significantly more than Dutch CFOs on average use more sophisticated capital budgeting technique than Chinese CFOs do.

ITURRALDE SR, MASEDA SR, JOSE AND ITURRALDE SR, (2005) provided an overview of corporate treasury management, which is the application of cash management. This article contributed to the ongoing debate in financial literature by analyzing the extent to which the size of corporations, the sectors in which they operate and the training of financial decision – markets influence treasury management, seeking to maximize results obtained by the treasury department and therefore to help maximize the value of the firm.

SAHOO AND OMKAR NATH (2005) analyzed the capital structure of Indian corporate sector and also, whether any shift has taken place in the financing liberalization in early 1990s. All those factors which determine the debt-equity choice of Indian private sector firms have been discussed. The study revealed totally different results as compared to studies in developed countries.

ASHBAUGH, COLLINS AND LA FOUND (2004) investigated the extent to which governance attributes that are intended to mitigate agency risk affect firms' cost of equity capital. The data used in the analysis covers seven fiscal years from 1996 to 2002. Governance attributes were examined along four dimensions: financial information quality, ownership structure, shareholder rights and board structure. Collectively, the governance attributes they

examined explain roughly 8% of the cross-sectional variation in firms' cost of capital and 14% of the variation in firms' beta.

BHOLE AND MAHAKUD (2004) presented a brief review of literature on theories of the corporate capital structure and analyzed the trends in the corporate capital structure in India in respect of public and private limited companies. Results show that leverage ratios generally have increased significantly during 1966-2000. Also, apparently, dependence of debt is more in case of public limited companies than private limited companies.

BAKER AND WURGLER (2003) developed a theory in which the decision to pay dividends is driven by investor demand and also recognized that managers cater to investor by paying dividends when investors put a stock price premium on payers and not paying when investors prefer non payers. To test this prediction, four time series measures of the investor demand for dividend payers was constructed for the period 1962-2000. By each measure, payers omit dividends when demand is low.

BHATTACHARYYA (2003) explained dividends as a component of a screening set up by an uninformed principal. The study starts with a well-documented empirical fact that there is a relation between dividends declared and executive compensation. It was uncovered that when hidden information is about the productivity of the agent then dividend – conditional on cash availability – bears an inverse relationship to managerial type.

DELOOF (2003) investigated the relation between working capital management and corporate profitability. The study took a sample of 1009 large Belgian non-financial firms for the 1992-1996 periods. Trade credit policy and inventory policy were measured by number of days account receivable, accounts payable and inventories and the cash conversion cycle was used as a comprehensive measure of working capital management.

DROBETZ AND FIX (2003) test leverage predictions of the trade-off and pecking order using Swiss data. At an aggregate level, leverage of Swiss firms is comparatively low, but the results depend crucially on the exact definition of leverage. Confirming the pecking order model but contradicting the trade – off model, more profitable firms use less leverage. Firms with more investment opportunities apply less leverage, which support both the trade –off model and a complex version of the pecking order model.

Leverage is also closely related to tangibility of assets and volatility of a firm's earnings. Finally, estimating a dynamic panel model, Swiss firms were found to maintain target leverage ratios. It was also observed that leverage has been slightly decreasing during the last decade.

GODE AND MOHANRAM (2003) tested the empirical predictions of the (Ohlson – Juettener, 2000) cost of equity capital estimates and compared this model with the residual income valuation (RIV) model in a predictive setting. The OJN model relates the current price (P_0) to forthcoming earnings (eps_1), forthcoming dividends per share (dps_1), two-years-ahead eps

(eps 2) and as assumed perpetual growth rate (γ). The study concluded that the RIV model generally outperforms the OJN model in predicting one year –ahead implied risk premia and realized returns potentially because the former incorporates additional information, particularly the industry median ROE.

HOWORTH AND WESTHEAD (2003) examined the working capital management of small companies in the UK. The study applied Principal components analysis and cluster analysis and the results confirm the identification of four distinct ‘type’ of companies with regard to patterns of working capital management. The first three ‘type’ of companies focused upon cash management, stock or debtors routines, respectively, whilst the fourth ‘type’ was less likely to take up any working capital management routines. Multinomial logistic regression analysis suggested that the selected independent variables successfully discriminated between the four ‘types’ of companies.

LEE, NG AND SWAMINATHAN (2003) employed data from G-7 countries to (a) devise a practical approach to estimating the cost of equity capital to aid in international investments and (b) to conduct tests of international asset pricing model (IAPM) using forward- looking cost of equity capital measure .

MARQUES AND SANTOS (2003) examined theoretically and explored empirically the problem of the banking firm’s capital structure (voluntary) decisions during 1989-1998. Findings support the notion that Portuguese banks’ debt/equity choice do matter. Results also indicate that surveyed CEOs show a relative preference for the trade-off capital structure policy model. Survey results are consistent with a number of theoretical propositions typically associated with the determinants of debt-equity choice of non-financial firms.

NAGANO (2003) investigated micro-economic variables that determined corporate capital structure in the East Asian countries of Indonesia, Korea, Malaysia, the Philippines and Thailand in the aftermath of the 1997 Asian financial crises.

MEDEIROS (2003) tested the validity of Fleuriet’s model, also known as Advanced or Dynamic Working Capital Analysis. The study used statistical and econometric methods involving correlation analysis and cross-section and panel data regressions.

RUBACK AND SESIA (2003) worked on working capital management of Dell Computer Corp. which manufactures, sells services personal computers. The company markets its computers directly to its customers and builds computers after receiving a customer order.

DESAI, FOLEY AND HINES JR.(2002) analyzed dividend remittance by a large panel of foreign affiliates of U.S. multinational firms. The sample consists of 10,838 affiliates with 1,347 parent companies during 1982-1997. The dividend policies of foreign affiliates, which convey no signals to public capital markets, nevertheless resemble those used by publicly held companies in paying dividends to diffuse common shareholders.

MACKAY AND PHILLIPS (2002) examined how intra-industry variation in financial structure is related to industry factors. An unbalanced panel of 4,248 firms operating in 142 competitive industries in the period 1981-2000 was analyzed by applying OLS and GMM of regression to data.

OMET AND MASHHARAWA (2002) examined the nature and determinants of the capital structure choice of Jordanian, Kuwaiti, Omani and Saudi Arabian non-financial listed companies. Based on the time period 1996-2001, the results indicate that the Jordanian, Kuwaiti, Omani and Saudi Arabian companies have low leverage ratios.

GRAHAM AND HARVEY (2002) analyzed a comprehensive survey that describes the current practice of corporate finance. The paper identified areas where the theory and practice of corporate finance are consistent and areas where they are not. Capital budgeting and capital structure decisions were explored in depth, asking approximately 100 questions. The sample consisted of a large cross-section of approximately 4,440 firms. In total, 392 Chief Financial Officers responded to the survey, for a response rate of 9%.

READY (2002) examined the dividend behavior of Indian corporate firms over the period 1990-2001 and attempted to explain the observed behavior with the help of trade-off theory and signaling hypothesis. In the study, dividend trends of a large sample of stocks traded on the NSE and BSE were analyzed, which indicate that the percentage of companies paying dividends has declined from 60.5% in 1990 to 32.1% in 2001 and that only a few firms have consistently paid the same levels of dividends. Results demonstrate that dividend changes appear to signal contemporaneous and lagged earnings performance rather than the future earnings performance.

SATHYAMOORTHY (2002) discovered the relative importance of various current asset companies for co-operatives in Botswana. The study covered the period of 1994-97. The results show that the co-operatives had low liquidity resulting into delay in paying off short-term debt. The study demonstrates that almost 45% of their current assets were sunk in stock. The cash holding was around 39% in all the four years. Finally, it was established that the societies adopted a conservative policy during the period under study.

AKALU AND TURNER (2001) examined the capital budgeting practices of four companies operating in different industry. The findings indicate that most companies follow decentralized project decision-making. Despite the use of DCF techniques, there is a tendency to combine with the newly crafted value management tools, which shows a trend shift in the capital budgeting methods.

BHATTACHARYYA AND BANERJEE (2001) examined the explanatory powers of three broad categories of factors in shaping corporate financial policy in Indian scenario. The study established that contracting costs and information costs have more telling effect in corporate debt policy than tax issues.

HALL (2001) stated that in determining the feasibility of projects where capital investments are concerned, various methods are used. The main objective of this study was to investigate the importance of risk with regard to capital investment projects. Secondly, with the aid of an empirical study, the study tried to establish whether risk is incorporated when South African companies evaluate capital investment projects. The empirical analysis indicated that risk analysis and evaluation in practice are to a large extent neglected by South African companies.

BOTOSAN AND PLUMLEE (2001) estimated the expected cost of equity capital using the unrestricted form of classic dividend discount formula and examined the extent to which these estimated (rDIV) reliably proxy for expected cost of equity capital. It was located that the rDIV estimated are associated with six risk proxies (Increasing in leveraged market beta. Increasing, decreasing or unrelated to leverage, after controlling for leveraged market beta. Decreasing in firm size, Increasing in book-to-price, Increasing in long-term growth, Decreasing in price momentum). Also, it was observed that the rGORDON estimates have the highest correlation with rDIV and behave in a manner consistent with expectations with respect to their relationships with the risk proxies.

GEBHARDT, LEE AND SWAMINATHAN (2001) proposed an alternative technique for estimating the cost of equity capital. The study used a discounted residual income model to generate a market implied cost-of-capital. Using 18,612 firm-year observation from 1979-1995, study shows that a firm's implied cost-of-capital is a function of its industry membership, B/M ratio, forecasted long-term growth rate and the dispersion in analyst earnings forecasts. Multivariate regression of implied risk premium on firm characteristics (sign of the coefficients in parentheses) show that, long-term growth in earnings (+), book to market ratio (+), industry membership proxies by average industry implied risk premium (+) and dispersion in analysis forecasts (-) are significantly related to risk premium. Together, these variables explain around 60% of the cross-sectional variation in future (two-year-ahead) implied costs-of-capital.

BABU AND JAIN (2000) examined the significance in industry class in designing capital structure of Indian private corporate enterprises. The study is based on sample of 527 manufacturing corporations for the period 1980-1994.

BEVAN AND DANBOLT (2000) analyzed the dynamic in capital structure for UK companies from 1991 to 1997. Significant changes were observed in the relative importance of various debt elements over time, as well as changes in the relationship between gearing and the level of growth opportunities, company size, profitability and tangibility.

BOTOSAN AND PLUMLEE (2000) observed the association between expected cost of equity capital and three types of disclosure (annual report, quarterly and other published reports and investor relations). The sample consists of 3,620 firm year observations from 1985-86 to 1995-96.

The study found that r_{EBO} estimates are highly correlated with and economically similar to the theoretically correct r_{DIV} estimates. R_{GORDON} estimates are also highly correlated with r_{DIV} , however the estimates produced by this approach significantly understate cost of equity capital. Finally, r_{GLS} estimates are not highly correlated with r_{DIV} and significantly understate cost of equity capital. It was concluded that cost of equity capital is decreasing with annual report disclosure level. Surprisingly, a positive association between cost equity capital and the level of more timely disclosures, such as the quarterly report was found.

DAS AND ROY (2000) investigated empirically the existence of inter-industry differences in the capital structure of Indian firms and the analysis covers the pre and post – liberalization periods separately to indicate if there is a clear break in the financing pattern of the Indian firms due to the policy shift. Twelve Indian industries were analyzed using one way analysis of variance technique.

DEANGELO AND SKINNER (2000) analyzed the information content of special dividends and firms' general tendency to increase regulars when they reduce specials and also examined the relation between institutional ownership and the payment of special and investigated the connection between repurchases and the decline in specials. The study examined the special dividends declared from mid-1962 (when daily stock returns become available on CRSP)through year-end 1995 by NYSE firms. Evidence suggests that firms that stop paying specials substitute into more frequent regular increases but do not alter the pattern of total dividends (per the Lintner (1956) model). Firms that reduce specials tend to increase regulars, effectively making the two types of dividends closer substitutes (and this tendency is more pronounced in recent years). Finally the research concluded that special dividends were not displaced by stock repurchases, indicating that most specials failed to survive on their own accord and not because managers discovered the tax advantages of repurchases.

WU (2000) examined the strategic role of “cost of capital” in residual income measurement in anoligopoly. Facing a stochastic production – technology with diminishing marginal return in the decision context of capital investment, firm owners can use the “cost of capital” in residual income measures as a competitive tool for their managers. It has been explained that the mode of competition (i.e. Cournot versus Bertrand) has a significant impact on the strategic role and determine whether the firm owners levy a lower or higher “cost of capital” on their managers than their own opportunity cost of capital. Finally, it is concluded that in the decision context of capital investment, this strategic role depends upon the mode of imperfect competition and the sources of uncertainty.

COLLINS, PINCUS AND XIE (1999) find that value effect of earnings is smaller in the negative-earnings region than in the positive-earnings region, which cannot be explained by a simple linear model. They also find value to be negatively correlated with earnings among firms with negative earnings which seems to contradict the conventional earnings-capitalization model.

KAKANI (1999) provided an empirical examination to widely held existing theories on the determinants of corporate capital structure and their maturity. A new model on capital structure was also developed for large manufacturing firms in developing economies such as India.

KOEDIJK ET AL.(1999) empirically investigate to what extent three competing asset pricing models price an individual firm's stock differently in an internationally integrated world. Formal statistical tests were derived for the existence of a pricing error of the domestic CAPM versus both the single factor ICAPM and the multifactor ICAPM. The significance of these pricing errors was tested in a sample of 2,483 firms from 10 industrialized countries using monthly data from 1980 to 1995. It was located that the single factor ICAPM without exchange rate factor induces erroneous pricing for more than 60% of all firms. The domestic CAPM leads to a substantial and statistically significant pricing error for approximately 7% of all firms. In an integrated world the cost of capital should be determined using the international capital asset pricing model (ICAPM) rather than the domestic capital asset pricing model (CAPM).

BRUNER, EADES AND HIGGINS (1998) presented the results of a cost-of-capital survey of 27 highly regarded corporation, ten leading financial advisers and seven best selling textbooks and trade books. The study found large variation, however, for the joint choices of the risk-free rate, beta and the equity market risk premium as well as for the adjustment of capital cost for specific investment risk. The study summarizes that CAPM is currently the preferred model for estimating the cost of equity. Betas are drawn substantially from published sources preferring those betas using a long interval of equity returns. Choice of an equity market risk premium is the subject of considerable controversy both as to its value and method of estimation. Most of best practice companies use a premium of 6% or lower while many texts and financial advisers use higher figures. Penman (1998) asserted that it is common to apply multipliers to book value of equity and earnings to calculate approximate equity value.

COLLINS, SAXENA AND WANSLEY (1996) explicitly recognized the potential differences in dividend policy between regulated and unregulated firms and focuses on agency-cost and monitoring explanations for the relevance of dividends. The study examined the role of insiders in determining dividend policy for unregulated firms, utilities and financial-services firms and it was recognized that insiders play a reduced role in determining dividend policy of utilities and financial services firms compared to unregulated firms. The sample consists of observations on 500 firms drawn randomly from edition 1-10 of Value Line Investment Survey dated December 22, 1989, through March 16, 1990.

KATO, KUNIMURA AND YOSHIDA (1996) observed whether Japanese banks had managed earnings from fiscal year 1981 to 1991 in order to comply with dividend guideline by Japanese Ministry of Finance. The guideline, a core policy for capital adequacy of banks, limited the upper bound of dividend payout ratio within 40% of current net income and was effective until its suspension in August 1992.

CONSTAS, MICHAEL (1995) examined the relationship between earnings, dividend declaration and investor returns. The empirical results of their study suggest that most of the information contained in dividends, which is useful to financial markets, is also contained in accounting earnings. But, there does appear to be some useful information in dividends that is not contained in accounting earnings.

JOG AND SRIVASTAVA (1995) provided the direct empirical evidence on the capital budgeting process including estimation of the cost of capital based on a survey of 133 large Canadian companies. Our results indicate that the use of DCF methods has become norm. Our respondents report high use of subjectivity and judgment in the estimation of inputs into the capital budgeting process, reflecting its strategic nature. Subjective management estimates are used as much to generate cash flow forecast as the more sophisticated quantitative methods. Similarly, although WACC seems to be the preferred discount rate, determination of the cost of equity is mainly judgmental.

RAJAN AND ZINGALES (1995) investigated the determinants of capital structure choice by analyzing the financial decisions of public firms in major industrialized countries. They found that at an aggregate level, firm leverage is fairly similar across the G-7 countries. It was also found that factors identified by previous studies as correlated in cross-section with firm leverage in the U.S., are similarly correlated in other countries as well.

SLOVIN, SUSHKA AND POLONCHECK (1994) assessed the information conveyed by commercial bank announcements of dividend reductions. It has been established that valuation effects on announcing banks are negative and significantly greater than for industrial firms. Cross-sectional regressions used in the study indicate that the size of dividend reductions is crucial but there is no evidence of clientele effects.

KARAK, H (1993) examined the policy decision regarding divisible profit and dividend decision. The study concludes that management in India, as a rule, has recently followed conservative policies with regard to dividends. There is an increasing tendency on their part to finance the expansion out of internal resources as far as possible.

ALLEN (1991) reports the results of an investigation of financial managers' perceptions of the broad determinants of listed Australian company capital structure decisions. The research method involves a series of field interviews undertaken with the company secretaries and senior financial personnel of 48 listed Australian companies.

ROSS (1986) shed light on the difference between theory and practice in the implementation of DCF analysis. Data were gathered, in 1982-85, from 15 large firms with three each from the steel, paper, chemical, aluminum and petroleum refining industries. Survey of capital budgeting practices among large firms has indicated a widespread use of discounted cash flow (DCF) methods, especially internal rate of return. At the same time, many firms state that they also

continue to use simple payback or related methods. Survey has shown that many firms use either a weighted average cost of capital or the cost of a specific source of funds in determining a hurdle rate. Most firms, however, employ some form of capital rationing –that is, they restrict capital expenditures even though it generally means neglecting profitable projects.

DHAMEJA (1978) in his study tested the dividend behavior of Indian companies by classifying them into size group, industry group, growth group and control group. The sample included 158 non-government public limited manufacturing companies listed on various Indian Stock Exchanges. The study found that there was no statistically significant relationship between dividend payout, on the one hand and industry and size on the other. Growth was inversely related to dividend payout and was found to be significant.

KUMAR (1976) made an attempt to examine the influence of some of the major determinants of dividend payment, particularly the target payout ratio, in the corporate sector of India. The study is confined to four industries: General Engineering, Chemical, Electrical and cotton Textile covering a period of three years: 1969, 1970 and 1971. The well-known Lintner's model and Brittain's cash flow model have been tried. The study result discloses that both in chemicals and general engineering industries, the earnings and cash flow variable along with lagged dividend variable seem to explain a large part of the variation in the dividend payout ratio. However in electrical and cotton textile, the earnings hypothesis explains the dividend variation better.

CONCLUSION

The concept of Corporate Finance focuses on the key objective of the firm being shareholder value creation. It has various sub-areas developed and analyzed in detail and various forms by numerous scholars. From the appraisal of various studies on the subject under reference, it is evidently clear that the concept has got sorted out in diverse ways over time. Graham and Harvey (1999) made a survey about the cost of the capital, capital budgeting and capital structure and described the current practice of corporate finance. In their words, "Our survey of the practice of corporate finance is both reassuring and puzzling". Therefore, even after five decades of seminal work of Modigliani and Miller (1958), there still remain gap to be filled. P.K. Jain, N. Bhattacharyya, Manoj Anand, Ashok Benerjee, L.M. Bhole and Jitendra Mahakud are among the leading Indian researcher who have carried out a range of empirical studies vis-a-vis corporate finance. However, no study has been conducted concerning corporate finance practice of Indian Banking and Information Technology Industry as such. Therefore, the study seeks to improve the understanding of academicians and practitioners regarding capital budgeting cost of capital, capital structure, working capital and dividend decisions of these two industries.

REFERENCES

Akalu, Mehari Mekonnen and Rodney Turner (2001), "The Practice of Investment Appraisal: An Empirical Enquiry", ERIM Report Series Research In Management, Reference Number ERS – 2001-77-ORG.

Allen, D. E., (1991), "The Determinants of the Capital Structure of Listed Australian Companies: The Financial Manager's Perspective", www.agsm.unsw.edu.au/eajm/9112/pdf/allen.pdf.

Anand, Manoj and Malhotra, Keshav, (2007), "Working Capital Performance of Corporate India: An Empirical Study", ICAI Journal of Applied Finance, Vol. 13, No. 1, pp. 46-81, January.

Ashbaugh, Hollis, Collins, Daniel W. and LaFond, Ryan, (2004), "Corporate Governance and the Cost of Equity Capital", [Papers. Ssn.com/sol3/paper.cfm?abstract_id=639681](http://papers.ssrn.com/sol3/paper.cfm?abstract_id=639681)

Babu, Suresh and Jain, P.K. (2000), "The Influence of Nature of Business on Corporate Debt Ratios- Empirical Evidence from Indian Private Corporate Sector", Finance India Vol. XIV No. 4, December, pp. 1165-1173.

Baker, Malcolm and Wurgler, Jeffrey, (2003), "A Catering Theory of Dividends", <http://www.nber.org/papers/w9542>.

Barclay, M. and C. Smith, (2005), "The Capital Structure Puzzle: The Evidence Revisited", Journal of Applied Corporate Finance 17, pp. 8-17.

Bauer, L. and Bhattacharyya, N., (2006), "Rethinking Lintner: An Alternative Dynamic Model of Dividends", http://hermes.ssrn.com/sol3/papers.cfm?abstract_id=914197.

Bevan, A. and Danbolt, J., (2000), "Dynamics in the determinants of capital structure in the UK", Working paper, University of Glasgow.

Bhattacharyya, Malay and Banerjee, Ashok, (2001), "Determinants of Capital Structure Revisited Empirically", The ICAI Journal of Applied Finance, Vol. 7, No. 2, April, pp. 38-53.

Bhattacharyya, N., (2003), "Good Managers Work More and Pay Less Dividends- A Model of Dividend Policy", http://paper.ssrn.com/sol3/paper.cfm?abstract_id=114608.

Bhattacharyya, S. K. and Raghavachari, M., (2005), "Determinants of Effective Working Capital Management- A Discriminant Analysis Approach", Indian Institute of Management Ahmedabad, Research and Publication Department, IIMA Working Paper 151.

Bhole, L.M. and Mahakud, Jitendra (2004), "Trends and Determinants of Corporate Capital Structure in India: A Panel Data Analysis", Finance India, Vol. XVIII, No. 1, March, pp. 37-55.

Botosan, Christine A. and Plumlee, Marlene A. (2000), "Disclosure Level and Expected Cost of Equity Capital: An Examination of Analysis' Rankings of Corporate Disclosure and Alternative Methods of Estimating Expected Cost of Equity Capital", http://papers.ssrn.com/paper.taf?abstract_id=224385

Botosan, Christine A. and Plumlee, Marlene A. (2001), "Estimating Expected Cost of Equity Capital: A Theory- Based Approach", [paper.ssrn.com/sol3/paper.cfm?abstract_id=279309](http://papers.ssrn.com/sol3/paper.cfm?abstract_id=279309).

Bruner, Robert F., Robert, Kenneth M. and Higgins, Robert C. (1998), "Best Practices in Estimating the Cost of Capital: Survey and Synthesis", *Financial Practice and Education*, Spring/ Summer, 13-28.

Buferna, Fakher, Bangassa, Kenbata and Hodgkinson, Lynn, 2005, "Determinants of Capital Structure Evidence from Libya", No. 2005/08, *Research Paper Series, Management School*.

Christoffersen, Peter, Jacobs, Kris and Vainberg, Gregory (2006), "Forward- Looking Betas", papers.ssrn.com/sol3/papers.cfm?abstract_id=891467.

Collins, M. Cary, Saxena, Atul K. and Wansley, James W., (1996), "The Role of Insiders and Dividend Policy: A Comparison of Regulated and Unregulated Firms", *Journal of Financial and Strategic Decisions*, Summer, volume 9, number 2.

Collins, D.; M. Pincus; and H. Xie, (1999), "Equity Valuation and Negative Earnings: the Role of Book Value of Equity", *The Accounting Review* 74, pp.29-61.

Constas, M. (1995), "Essays on the Relationship between Stock Prices, Dividends and Accounting Earnings", *D.A.I.*, vol. 56, No. 1, pp.258 A

Das, Sumitra and Roy, Malabika, (2000), "Inter-Industry Differences in Capital Structure: The Evidence from India", [www.igidr.ac.in/ money/malabika.pdf](http://www.igidr.ac.in/money/malabika.pdf).

DeAngelo, Harry, DeAngelo, Linda and Skinner, Douglas J., (2000), "Special Dividend and the Evolution of Dividend Signaling", *Journal of Financial Economics*, 2000, 57(3), pp.309.

Deloof, Marc (2003), "Does Working Capital Management Affect Profitability of Belgian Firm?", *Accounting*, Vol. 30, No3&4.

Desai, Mihir A., Foley, C. Fritz and Hines Jr., James R., (2002), "Dividend Policy Inside the Firm", <http://www.nber.org/papers/w8698>.

Dhameja, N.L., 1978, "Control of Companies and their Dividend Practices", *Margin*, January. Drobetz, Wolfgang and Fix, Roger, (2003), "What are the Determinants of the Capital Structure? Some Evidence for Switzerland", WWZ/ Department of Finance, Working Paper No. 4/03.

Eny, Enyi Patrick (2005), "Applying Relative Solvency to Working Capital Management-The Break-Even Approach", <http://ssrn.com/abstract=744364>.

Gebhardt, W R , C M C, Lee and Swaminathan , B. (2001), “ Toward an Implied Cost ofCapital”, *Journal of Accounting Research*, 39, pp.135-176.

Gode, D. and Mohanram, P. (2003), “Inferring The Cost of Capital Using The Ohlson-JuettnerModel”, *Review of Accounting Studies* , 8,pp.399-431.

Graham, J. and C. Harvey, (2001), “The Theory and Practice of Corporate Finance : Evidencefrom the Field”, *Journal of Financial Economics* 60, pp.187-243.

Graham, John R. and Harvey, Campbell, R. , (2002), “How Do CFO’s Make Capital Budgetingand Capital Structure Decisions ?” *The Journal of Applied Corporate Finance* , Vol. 15, No.1.

Gropp, Reint and Heider, Florian (2008). *The determinants of capital structure ; Some evidence from banks. Discussion Paper No. 08-015, Zew Research*, <ftp://ftp.zew.de/pub/zew-docs/dp/dp08015.pdf>
Accessed on March 20,2008.

Habib, Ahsan (2005), “Information Risk and the Cost of Capital : Review of the EmpiricalLiterature”,
http://papers.ssrn.com/sol3/papers.cfm?abstract_id=722781.

Hail, Luzi and Leuz, Christian (2006), “International Differences in the Cost of Equity Capital:Do Legal Institutions and Securities Regulation Matter ?” *Journal of Accounting Research*, June.

Hall, J. H. (2001), “The Incorporation of Risk in the Capital Investment Decision”,
http://papers.ssrn.com/paper.taf?abstract_id=243163.

Hermes, Neils, Smid, Peter and Yao, Lu, (2005), “Capital Budgeting Practices: A ComparativeStudy of the Netherlands and China”

Howorth, Carole and Westhead, Paul (2003), “ The Focus of Working Capital Management inU K Small Firms” , *Management Accounting Research*, Vol.14, No. 2, June.

Iturralde Sr. Txomin, Maseda Sr. Amaia, Jose, Leire San and Iturralde Sr, Txomin (2005), “ The Cash Management Routines: Evidence from Spanish Case”,<http://ssrn.com/abstract=728365>.

Jain, P K and Kumar, Praveen (2006), “Working Capital Management Practices- A Study ofNifty Index Companies”,*JIMS 8M*, July- September, pp.4-21.

Jog, Vijay M. and Srivastava, Ashwani K. (1995), “Capital Budgeting Practices in CorporateCanada”, *Financial Practice and Education*, Fall/ Winter 1995.

Joos, Philip and Zhdanov, Alexei, (2007), “Earnings and Equity Valuation in the BiotechIndustry : Theory and Evidence”, <http://ssrn.com/abstract=987924>.

Kakani, Ram Kumar, (1999), "The Determinants of Capital Structure- An Econometric Analysis", Finance India , Vol. XIII No. 1, March, pp. 51-69.

Kannadhasan, M. (2007), "Working Capital Management in a Public Limited Company- A Case Study", The ICAI Journal of Management Research, Vol. 6, No. 5, pp. 20-33, May.

Karak, H. (1993), "Dividend Profit and Dividend Decision", the Management Accountant, March 1993, pp. 235-237.

Kato, Kazuo, Kunimura, Michio and Yoshida, Yasushi, (1996), "Discretionary Behavior of Banks' Earnings and Banks' Dividend Guideline in Japan", www3.bus.osakacu.ac.jp/apira98/archives/pdfs/45.pdf

Koedijk, Kees G. , Kool, Clemens J.M., Schotman, Peter C., Van Dijk, Mathijs A. and Nissen, Francois G.J.A. (1999), "The Cost of capital in International Financial Markets: Local versus Global Beta", papers.ssrn.com/sol3/papers.cfm?abstract_id=166848.

Krishnamurthy, K. and Sastry, D. U. , (1975), "Investment and Financing in The Corporate Sector In India", Tata McGraw Hill Publishing Company Limited, New Delhi.

Kumar, S., (1976), " Corporate Dividends and Target Payout Ratios in India", in Business Economics and Planning, Edited by Ghose , Minocha and Gupta, Kalyani Publishers, New Delhi.

Lee, C. Ng, D. and Swaminathan, B. (2003), "The Cross- Section of International Cost of Capital", Working Paper, Cornell University.

Lintner, J. (1956), "Distribution of Incomes of Corporations among Dividends, Retained Earnings and Taxes", American Economic Review, 46, pp.97-113.

Mackay, Peter and Phillips, Gordon M. , (2002), "Is There An Optimal Industry Financial Structure?", <http://www.nber.org/papers/w9032>.

Marques, Manuel O. and Santos, Mario C. , (2003), "Capital Structure Policy and Determinants: Evidence from the Portuguese Banking Industry", http://www.fep.up.pt/investigacao/cempre/actividades/sem_fin/sem_fin_01/papers_pdf/paper_sem_fin_14nov03.pdf.

Medeiros, Otavio R. De (2003), "Questioning Fleuriet's Model of Working Capital Management on Empirical Grounds", <http://ssrn.com/abstract=700802>.

Miao, Jianjun, (2005), "Optimal Capital Structure and Industry Dynamics", The Journal of Finance, December 2005, Vol. Lx, No. 6.

Modigliani, F., and M. Miller, (1958), "The Cost of Capital, Corporation Finance and the theory of investment", *American Economic Review*, 48, pp. 261-275.

Morgan, Donald P. (1999), "Bank Commitment Relationships, Cash Flow Constraints and Liquidity Management", *FRBNY Staff Report No. 108*, January.

Nagano, Mamoru, (2003), "Determinants of Corporate Capital Structure in East Asia- Are their differences from the Industrialization Countries?", WIF-04-002, Working Paper Series, Institute of Finance, Waseda University.

Omet, Ghassan and Mashharawe, Fadi, (2002), "The Capital Structure Choice in Tax Contrasting Environments: Evidence from the Jordanian, Kuwaiti, Omani and Saudi Corporate Sectors", Working Paper Series, Faculty of Economics & Administrative Sciences, The Hashemite University, Jordan.

Pandey, I. M. and Chotigeat, T., (2006), "The Capital Structure of Asian Firms", *Global Business and Finance Review*, Spring, pp. 63-77.

Penman, S. H. (1998), "Combing Earnings and Book Value in Equity Valuation", *Contemporary Accounting Research* 15(3), pp.291-324.

Ponnaluru, Sreenivasa Suresh (1998), "Fixed Capital and Inventory Investment, Dividends and External Finance in India Sugar Industry- An Econometric Investigation in Search of their Determinants and Interdependence", *Finance India*, XII No 2, June, pp.440-442.

Raaballe, Johannes and Jakob Stig Hedensted, (2008), "Dividend Determinants in Denmark", http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1123436.

Rajan, R. and L. Zingales, (1995), "What Do We Know about Capital Structure? Some Evidence from International Data", *Journal of Finance* 50, pp.1421-1460.

Reddy G, Sudarsana and Reddy S, Raghunathan (2007), "Working Capital in Small Scale Industry", *SCMS Journal of Indian Management*, April-June, pp.48-55.

Reddy, Subba, (2002), "Dividend Policy of Indian Corporate Firms: An Analysis of Trends and Determinants", <http://nseindia.com/content/research/paper71.pdf>.

Ross, Marc, (1986), "Capital Budgeting Practice of Twelve Large Manufacturers", *Financial Management* (Winter 1986) Vol. 15, Issue 4, pp.15-22.

Rudback, Richard S. and Sesia, Aldo (2003), "Dell's Working Capital", *HBS Publishing Case No. : 9-201-029; Teaching Note No.: 5-201-017*

Sahoo, Sudhansu Mohan and Omkarnath G. , (2005), "Capital Structure of Indian Private Corporate Sector : An Empirical Analysis", *The ICFAI Journal of Applied Finance*, November, pp. 41-56.

Sathyamoorthi, C R (2002), "Management of Working Capital in Selected Co-operative in Botswana", Finance India, Vol. XVI No. 3, September, pp. 1015-1034.

Slovin, Myron B., Sushka, Marie E. and Polocheck, John, (1994), "Dividend Reductions and Commercial Banks", http://papers.ssrn.com/sol3/papers.cfm?abstract_id=5739.

Truong, Giang, Peat, Maurice and Graham Partington, (2007), " Cost of Capital Estimation and Capital Budgeting Practice in Australia", http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1019962

Wu, Martin G H, (2000), " The Strategic Role of "Cost of Capital" in Residual Income Measurement", http://papers.ssrn.com/sol3/papers.cfm?abstract_id=250165.