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Capital Structures: Towards Realizing Economic Growth

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Abstract: The econometric techniques provide the ground on which capital structures play a leading role in determining economic growth. This research explores the correlation of earning growth, realized growth as well as asset growth by the aspect of capital structures on the companies listed on stock exchange in the consumer goods industry in China. The interplay of economic factors and policy dimensions to the existing financial environment impacts on the general economy therefore, capital structures emerges as hinged on the existing financial condition index for the primary purpose of measuring the economic stability of the consumer goods companies. The results show the dynamics into the implementation of economic models of capital structures to indicate that in the past 20 year, the country's economy has grown steadily. While there are constraints of economic growth that will characterize the Chinese pathway, efforts to tackle efforts in improving savings, curbing corruption and improving the microeconomic conditions, it is predictable that the growth rate for China's economic trajectory will be increased.

Key words: Econometic techniques, capital structures, interplay, stability, chinese pathway, predictable

INTRODUCTION

World Bank projections show that China is among the fasted growing economy around the globe. This is evidenced with the average growth rate of 10% in the next three decades. In light of this, it is characteristic that as the biggest exporter of goods, it is likely to experience rapid economic growth. This growth will introduce a series of challenges that include challenges of environmental sustainability, high inequity as well as other external imbalances. Compared to the rest of the world, China's growth of income per capita is much quicker. Socially and economically, China has benefited greatly from Economic growth With regard to this, it is plausible to not that if no savings is done, investments are restricted and henceforth, insignificant economic development is expected to take place. However, if the savings level is misused on investment projects that are not productive. However, the extent of saving is not the only the vital thing but as well as the economic monitoring of investment resources.

Theoretical implication

Investment opportunity set theory: Investors interested in investing in trade practices must perceive the flourishing individual with their own capital to invest (Tan and Ma, 2016). Increased affluence of globalized market means that an increased number of disposable income and therefore they can spend on products offered by foreign investment companies offering personal products, food and household products. As already intimated, one of the major reasons why countries should engage more in foreign direct ventures is the fact that the middle class has experienced increased prosperity in recent years which creates new market opportunities. The increases affluence of the purchasing and economic power is establishing a new market for retailers in the western world who previously perceived the nation as a supplier of goods (Jennings and Velasquez, 2015). In addition to this, there are many market opportunities to be exploited by companies that offer financial and insurance services, cosmetics and automobiles. This is due to the fact that the market has burgeoned greatly in the last couple of years.

The most recent global financial crisis began in 2007 but gathered pace and spread with great intensity in 2008, in spite of the different actions and attempts of central banks and regulators to restore economies to the levels that were reigning previously (Liu and Maula, 2015). Stock markets fell around the world, large financial institutions have collapsed or were been bought out. The various news concerning the effects of the financial crisis and the inability of the various policies to deal with it have led to questions regarding the various causes of the financial crisis and how the various market structures propagate or help in its containment.

The recent global financial crisis can also be attributed to the various financial innovations in the financial markets. These systems were developed so rapidly in such a way that the systems of the market and market infrastructure were not prepared to spring into action when the instruments were under stress (Hunt *et al*., 2016). The complexities that resulted from the new financial instruments innovations led to three distinct effects especially on the investors. The regulators were confounded; the risks that were inherent in the market were hidden from the view of the various investors in the market and there was also confusion on the investors regarding the various merits and demerits of the investments that they wanted to commit to Tatarynowicz *et al.* (2016). This happened even though in the standard economic theory there is the notion that the investors always act rationally and that they would only get into risks that they completely understand. The lack of complete market knowledge led to the beginning of the crisis which later affected the whole globe.

Finally, there is the issue of off-balance sheet finance where many different banks and financial institutions kept special purpose entities which were not recorded in the balance sheets for example the Structure Investment Vehicle so that they could be able to engage in speculative behaviour (Lekovic and Maric, 2016). The banks were able to get more loans while at the same time; they created liabilities that were greatly worsened by the shocks that hit the financial market after the collapse of the subprime financial market. The effect was the loss of faith and trust in the financial institutions thus greatly affecting the creditworthiness of the banks. The investors therefore had a very little ability to know the true position of the various financial positions of the banks and financial institutions that they were dealing with. Rather than bring the benefit of managing the risks of the financial institutions, the finance in the off-balance sheet led exuberated the state of the financial crisis.

Strategic trade theory in financial crisis: The tenets of strategic trade theory shapes the thinking that countries must adopt business and economic policies in a bid to enhance their trade interaction between firms and other states in the international market. According to Idrisov and Murylev (2016), it becomes imperative to note that trade policies are informed with the shifting positions in the international trade practices pegged on the issues of import tariffs, subsidies, research and development, cultural factors as well as competitive and comparative advantage. Through the principles of strategic trade theory, countries should engage in foreign direct investment in the other countries and with other multinational corporations. This pegged on the understanding that the increasing prosperity of the country's trade practices have created new market opportunities in across the world. With regard to this, it is evident that firms and countries stand to benefit from trade practices presenting foreign direct investors with low costs of manufacturing.

The global retail business environment of the 21st century has undergone great transformations in comparison to what it was a century ago (Melnikas, 2013). The financial crisis that rocked the globe from the year 2008 greatly impacted the economies of the world particularly in the western world. The UK economy, however, benefited from the strength of its manufacturing and service industries and was therefore able to steer through the Global Financial Crisis (GFC) without much difficulty. Other important occurrences that have affected the economic and business situation in Australia is the increased strength of the Australian dollar and the liberalization of online shopping on both local and global contexts (Antoci *et al*., 2013).

MATERIALS AND METHODS

This research adopts a statisticalanalysis within the descriptivedimension. The multivariate and correlation regression analysis of data sufficed the appreciation of factors that affect the capital structures of companies in the consumer goods industry in China Stock Exchange. The selected companies were based on sales growth, earning growth and equity growth through the classification of relationship variables in the sample. The expectation of higher growth is pegged on the need for resources to finance growth through measures of capital structure.

Analysis

Capital structures correlations: Most consumer goods company are financed through a combination of long debt, retained profits, commercial paper, capital market issues, leases and bank borrowings. It is essential to note that the capital structure is not automatically impacted by all the increases in debt. According to financial propositions these alterations in capital structure are not supposed to impact on the firm's value but the company's return equity is supposed to improve (Yeung and Coe, 2015). Bogan (2012) notes that the first proposition posits that capital structure does not depend on independent while the second proposition outlines that shareholders should expect improvement on returns to equity when debt financing increases. Making the assumption of access to perfect markets, investors can themselves borrow for the purpose of achieving the same financial benefits that come with an organization's capital structure changes. From the outset, the two propositions appear to be incompatible but it is essential to note that improved returns get offset by the increase in risk, culminating in increased rate of return.

A case in point is Tesco. with regard to this, it is clear that shareholders are an indispensable finance provide despite the fact that during FY11, Tesco returned 900 m to them as dividends and bought back their own shares. This 900 m is indicative of one side of the changing capital structure of Tesco. with time companies

Table 1: Descriptive statistics of variables

Description	Maximum	Maximum	Middle	Average	Samples
The ratio of total debt	1/07	0/15	0/6772	0/6668	300
Long-term debt	0/68	0	0/0492	0/0826	300
Effectiv rate of tex	0/01	-0/28	-1/136	-1/085	300
Sales growth	11	-1/80	0/1585	0/2736	300
Firm size	7/73	4/47	5/5114	5/5999	300
Operational risk	185/03	-38/45	0/2877	0/8472	300
Asset-exactness	0/89	0	0/1816	0/2481	300

Table 2: Mean and median figures of different leverage measures

	Total liabilities/total assets		Total debt/total assests		Total debt/capital	
Years	Mean (%)	Median (%)	Mean (%)	Median (%)	Mean (%)	Meadian (%)
1992	83	85	68	69	79	83
1993	81	84	67	69	77	81
1994	79	82	66	68	75	78
1995	78	81	65	68	74	78
1996	78	81	65	68	74	78
1997	78	80	65	68	74	78
1998	78	80	65	68	74	77
1999	87	79	75	66	73	76
2000	75	78	63	65	71	75
Average	80	81	67	68	75	78

Total debt = short-term debt+long-term debt. Capital = total debt+book value of equity

are becoming less financed by equity and more by debt. The company also accesses finance through leases (Martin-de-Castro *et al*., 2011). Tesco's financial strategy regarding capital structure management is that it is planning to take capital from property assets to its shareholders. In addition the company is planning to increase its debt by £1.3 bn. This is expected to alter its debt-equity ratio through increasing debt within the capital structure. The transactions that will involve the company returning >1 bn capital to its shareholders will reduce it equity finance. Nonetheless, after the balance sheet, the company issued £986 m in bonds and increased payables by approximately £1 bn and lease commitments by around £1.4 bn.

Earning growth: The stated financial strategy of companies in this industry builds on the earning growth as well as sales growth by investing for growth in markets thus releasing capital from assets for shareholders returns. This reduces the company's dependence on equity finance. Companies reiterate that the intention of the company is freeing up capital from property assets for the purpose of offsetting future dilution of the company's earnings per share and making sure it is in a position to invest its CAPEX in growth (EH, 2015).

From the descriptive statistics in the table above, it is plausible to note that the records have further pointed out that the Chinese manufacturing cost advantage has significantly eroded over the period thereby leading to the rise in the costs of operating various businesses. In fact, specific details have pointed out that the cost of operating business in china have increased by a margin of between 25-30% since the period of 2005 and this has resulted in the development of increased performance (Gu and Lu, 2014). Certainly, the comparison of the manufacturing costs in China and in United States has proven to be identical and this has resulted in the transfer of the manufacturing hub from china to the United States where there is ample market. On the other hand, inflation has also affected the performance of the economy. The records from the economy has shown that the export market feel by 20.3% because the leading Chinese firms have lost to the more competitive Vietnam and other low cost competitors.

Equity growth: Equity growth in most consumer goods is reflected in the low debt-equity ratio. Most companies listed on the stock exchange are highly competitive based on the high market-book ratio. Therefore, financing of the firms is easily afforded through the firm's internal resources moving towards capital restructuring thus realize potential for returns on investments within the tenets of trade off theory (Bharti *et al*., 2015). Currently, the economic performance of China is on a steady trajectory with the tertiary industry likely to go up by 8.1%. The total value added of the industrial enterprises above designated size in 2014 was up by 10% at comparable prices, the annual growth of the heavy industry was 9.9 and 10.1% for the light industry. In addition, the number has been going up with an annual percentage of 4.3%. The trade balance recorded 231.1 billion dollars whereas the general trade of imports and exports total value was 2009.83 billion dollars, up by 4.4%. The yearly percentage of consumer price is 2.6%. However, this figure is 2.8% lower than the previous year. After price factors deduction, the per capita disposable income growth of urban households was 9.6% and was 1.21% higher than the previous year. This is clearly illustrated in Table 2.

Table 3: Summry statistics of the determinants

Determinant	Mean	Standard	Minimum	Maximum
Tanginility	0.288	0.220	0	1
Non-debt tax shield	0.055	0.048	0	1
Profitability	0.080	0.28	-10	14.324
Siz sale (MSEK)	41	280	0	99.956
Siz employment	158	737	0	41.398
Growth (%)	1.070	44.50	-1	4927
Uniqueness	0.009	0.338	0	64.6980
Income variability (%)	0.279	5.576	0	729.667
Total debt ratio	0.739	0.223	0	6.733
Short-term debt ratio	0.490	0.236	0	6.733
Long-term debt ratio	0.250	0.240	0	3.81

Sales growth: The financial policy is to smooth its debt profile, making sure that funding is arranged way ahead of time and retaining strong credit ratings. Although, the companies extensively mention these drivers in its FY11 report they do not emphatically state intent to alter the firm's capital structure. The obvious suggestion of the firm's policy is that as opposed to issuing shares, companies would only buy back shares, issue debt and pay dividends. The results of the research conducted in China have shown that the Chinese government is on the verge of experiencing higher manufacturing costs that are associated with the advancement in the wage rates (Rocca *et al*., 2011). Majority of the companies in the Chinese economy have experienced essential growth and are now operating under two-shifts given that the significant Chinese population provides the higher magnitude of the work force (Table 3).

Despite this development in the Chinese economy, the investors have asserted that they anticipated the critical rise in the wage rates and the detrimental impacts it pose to the economy. This depiction has significantly reduced the onsets of FDI which is normally identified as one of the leading income generators for the Chinese economy. The records have continued to add that China has significantly developed to overcome the dependencies of on the cheap labour. The implicit price index went up to 534.99 index points in 2010 from 501.64 index points in 2009. Since 1978, its GDP Deflator has been lying at 283.34 index points and reached an all-time high of 534.99 index points in June 2010 and a lowness of 100 index points in June 1978. Its most important components of the CPI basket are food at 31.8% total weight and residence 17.2% (Levine *et al*., 2012; Tan, 2014).

Empirical evidence: The global economy has continued to experience the aspects of growth and development because of the both technological and enhancement of the scope of knowledge towards management. In the wake of these developments, the leading economics have significantly experienced a rise in the performance of their economies. Particularly, Chinese economy has experienced critical growth and development to emerge as the second best economy across the globe (Nakamura, 2015). The increase in the growth and performance of the Chinese economy has significantly opened up the Chinese economy for the attributes of business and investments thereby increasing its aspect of performance. Despite this aspect of growth, the Chinese economy has experienced detrimental effects regarding the performance of the economy in the recent past (Purohit and Tandon, 2015).

The enactment of inappropriate policies has resulted in the decline in Chinese economic performance that is characterized by the weakening of the economy. The weakening of the economy is signified by the reduction in demand and the rise in the wage rates. In this regard, inflation and rising manufacturing costs are some of the leading detrimental factors that have continued to impact on the performance of the economy. The periods of the recent past has witnessed the critical rise in the wage rates with view of levelling with those in the United States (Dowd *et al*., 2015). This has increased the manufacturing costs and reduced the capacity of manufacturing in china. On the other hand, the reduction in PPI has also signified weakening of inflation and subsequent reduction in demand for the manufactured goods. In reality, these two factors illustrate most dangerous edge of china's economy thereby prompting the need for the enactment of corrective policies.

There is the complex securitization amplified the effects of the subprime mortgages. This risk was underestimated by the various rating agencies. The underestimation can be explained by a variety of factors for instance the inherent ability to establish the risk that were involved due to the complexity, lack of competition between the rating agencies and the poor or little accountability of the rating agencies (Mauldin, 2012). There was a general lack of knowledge coupled with the fact that there was a high rate of uncertainty regarding the presence where the securities with the bad mortgages were located. The different actors in the stock market did not have the slightest of ideas the various banks and financial institutions who were withholding the various bad mortgages.

The above scenario prompts a revaluation of the various components of the capital in the institutional regulatory and thus there will be an increase in the sales of the assets of the various institutions which will work to reduce the values of the assets of the firms further (Huggins and Strakova, 2012; Breit, 1964). The cycle continues under the watch of accounting and financial systems causing further effects on the financial market. The above scenario is driven to points of creating financial crisis by the various emotional and behavioural factors of the financial professional who have access to complete information about the financial markets but are constrained in their abilities by opacity of the information that they have.

RESULTS AND DUSCUSSION

As a result, the financial institutions will not have the agility and capacity to amplify the various stress factors. Also, they will not be able to have the magnitude as well as the speed that can be used to adjust to the various stress factors for instance spill over into financial markets and the default spreads. The effects of high dependency especially the interrelationship between the financial institutions for instance there are issues such as the interbank credit lines, connectivity, information linkages and interbank solvency exposures. Ssewamala (2015) explained that the lending relationships between the different financial institutions indicate how they will be affected by contagion. Secondly, concentration will lead to the breakdown of the networks especially in cases where financial institutions that are too big do not participate in the various market bailouts if the benefits that they will derive are less that the costs that they will incur if they did not participate in the bailout. This can be visualized as the beginning of the spiral which is then followed by a decrease in the liquidity reserves of the various financial institutions that are affected.

CONCLUSION

The financial crises can be attributed to the risky collaterals that were for instance the Japanese financial crisis was preceded by a lending policy that was greatly focused on the rising value of the land just as the crisis that originated from the United States where value was placed on the value of the property that were developed by the loans without the evaluation of the flows of cash. Most of the various financial crises are preceded by the depreciation of the value of the real estate. Real estate property can thus be considered as a very risky form of collateral that does not perform the function that it is required t do according to classical banking theory that states that the collaterals are supposed to reduce the risks of the banks. The boom and busts which characterize the real estate industry ensures that there are always swings which can lead to the collapse of the various financial institutions. The main problem here is that the collateral, the real estate property is an inside collateral therefore there is a high rate of failure of the subprime mortgage providers will incur high risks as a result of depreciation as the loans are used to finance the projects which may fail.

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