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IMPACT OF CAPITAL STRUCTURE ON PROFITABILITY:
WITH REFERENCE TO SELECT COMPANIES FROM OIL AND NATURAL GAS INDUSTRY OF INDIA

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ABSTRACT

The relationship between capital structure and profitability is an important matter of discussion as regular improvement in profitability is important for growth and survival of firm. An attempt has been made in this paper to find out impact of capital structure on overall profitability of a firm. The Corporate financial performance, which is represented by dependent variables ROA (Return on Assets) and Net Profit Ratio, is taken into consideration and the effect of independent variables which are Sales of a firm, Total Assets of a firm, Debt Service Capacity, Dividend Pay-Outs, Degree of Financial Leverage, Degree of Operating Leverage of the firms belonging to the Oil and Natural Gas Industry of India were chosen for study. A sample of seven firms listed in NSE and BSE were selected and the financial data of these companies during the period 2005 and 2015 is used for this study. The Judgement Sampling which is non-random sampling technique is chosen for sample selection in this study. The correlations and regression analyses were used to estimate the functions relating to profitability measured by Return on Assets and Net Profit Ratio with measures of capital structure. The study witness that Log sales, degree of operating leverage and growth of asset are significant variables in determining the profitability when dependent variables are ROA and log assets, degree of financial leverage, Log sales, degree of operating leverage and growth of asset have significant relationship with net profit ratio of the select firms from Oil and Natural Gas Industry of India.

KEYWORDS: *Capital Structure, Debt, Equity, Financial Ratios, Net Profit Ratio, Return on Assets.*

Introduction

"What will be an optimum capital structure for a firm?" has been one of the most difficult question to answer as well as the most crucial decision for every firm. The finance managers often find it difficult to conclude as to what will be the optimum capital structure for a firm which will reduce the cost of capital, will reduce tax liability optimally, will increase profitability, will fulfil the shareholders' expectations and will also ensure growth in future. According to Gerestenberg, "Capital Structure of a company refers to the composition or make up of its capitalization and it includes all long-term capital resources viz., loans, reserves, shares and bonds. Keown et al. defined capital structure as, 'balancing the array of funds sources in a proper manner, i.e. in relative magnitude or in proportions'. In the words of P. Chandra, 'capital structure is essentially concerned with how the firm decides to divide its cash flows into two broad components, a fixed component that is earmarked to meet the obligations toward debt capital and a residual component that belongs to equity shareholders".

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