

THE DYNAMIC NATURE OF OPTIMAL CAPITAL STRUCTURE: AN INTROSPECTION OF INDIAN FIRMS

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ABSTRACT

Firms all over the world are financed either through equity or external debt and this choice of equity and debt is what is known as the capital structure of a firm. The degree of dependency on external debt, determines the level of leverage of a firm. Even though theory suggests that ideally firms should stick to a fixed value of leverage in practice it is not so mainly due to the fact that the composition of each firm is unique and hence it makes sense that the capital structure of one firm is unique and not equivalent to all firms in general. There has been enough research on the desired optimal capital structure that a firm should adhere to. However, owing to the fact that not much research has taken place in the Indian context, this paper tries to analyze a pilot study on the determinants of capital structure which forms the base for a more in depth research on the topic by extending the study onto a broader database of Indian firms. The paper also touches upon a few relevant theories of capital structure which has been the base of research worldwide and summarizes the literature review of research already conducted on this topic.

KEYWORDS: Leverage, Capital structure, Indian firms, optimal, theories, Small Cap companies