The Project Life Cycle: Definition

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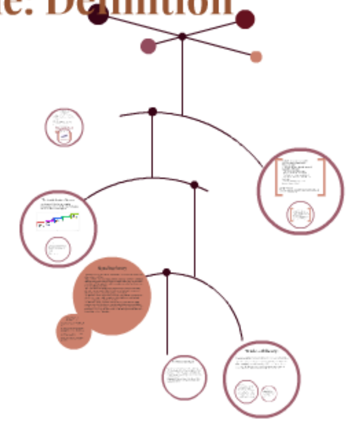

Conclusions

When regarding to a firm's capital structure, the Modigliani–Miller theorem opened a literature on the fundamental nature of debt versus equity. The capital structure of a firm is the result of the transactions with various suppliers of finance.

In the perfect capital markets world of Modigliani and Miller: the costs of different forms of financing do not vary independently and therefore there is no extra gain from opportunistically choosing among them. Nevertheless, financing clearly matters, and that as a consequence of taxes, differences in information and agency costs.

The various theories of capital structure differ in their interpretation of these factors. Each emphasizes some cost and benefits of alternative financing strategies, so they are not designed to be general.
According to the standard trade–off theory, taxes and bankruptcy account for the corporate use of debt.

According to the standard pecking order theory, adverse selection accounts for the corporate use of debt. Both theories having weak parts, it is not surprising that there is active research on this matter.

In the market timing theory, there is no optimal capital structure, so market timing decisions accumulate over time into the capital structure outcome. From this point of view, the market timing theory appears to have the most explanatory interest

Testing capital structure theories

Using data from 114 non-financial Jordanian firms (of which 62 are industrial firms and the remaining are services firms), we report evidence suggesting that:
Firstly, equity issues track the financing deficit relatively more closely, suggesting that equity is not the last resort for financing as the pecking order theory predicts
Secondly, Jordanian firms are more sensitive in retiring debt to take up surplus than in expanding debt to meet their financing requirement, implying that financial surplus and deficit affect leverage differently.
Thirdly, Jordanian firms have a target leverage ratio and adjust their leverage at rate higher for above–target leverage than for below–target leverage and at rate higher for firms with financial surplus than those with financial deficit.
Finally, we report evidence suggesting that the rates of adjustment vary depending on whether the deviation from the target level is large or small, with rates higher for large size deviation than for small size deviation

In Jordan, the banking system is well developed, although the financial market is still developing. Therefore, credit facilities from banks play a key role in financing Jordanian firms' investment. Consequently, it is important to identify the impact of market imperfections on the Jordanian firms' capital structure behavior. Several theories attempt to explain corporate financing behavior, including: trade off theory, agency cost theory, and pecking order theory

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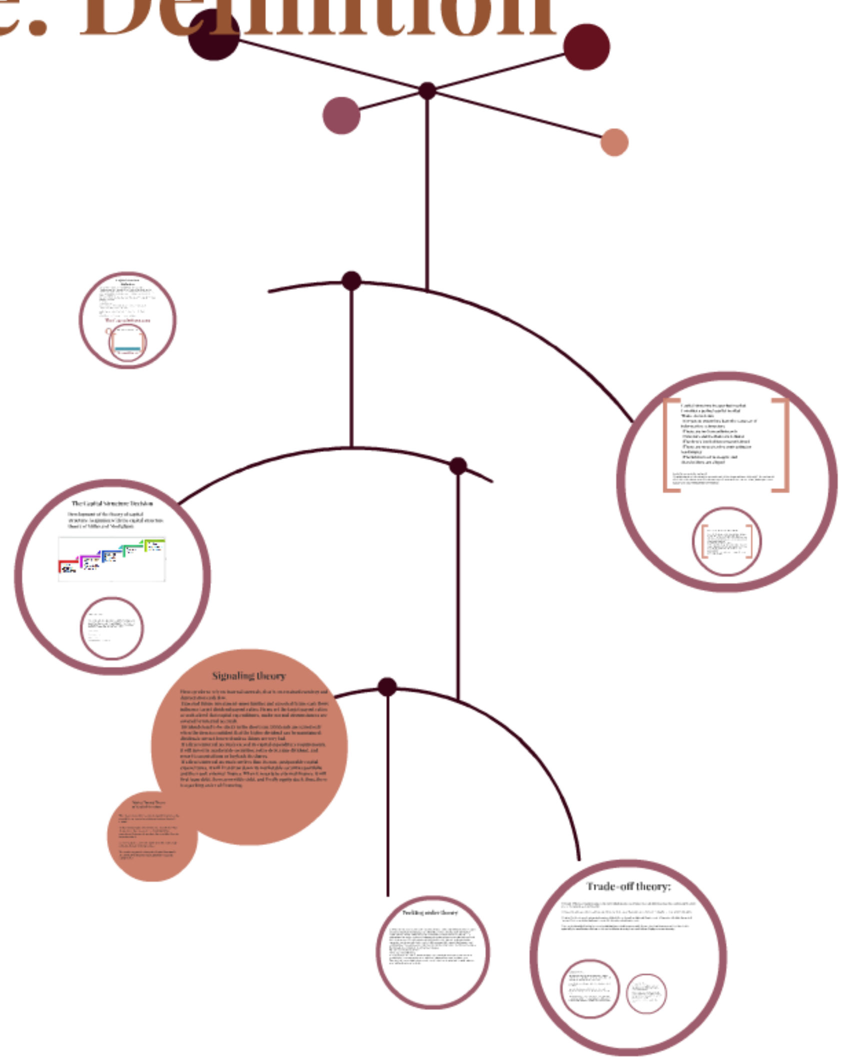
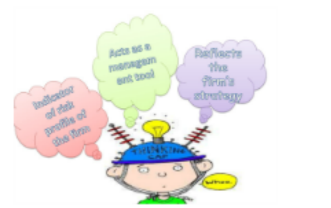


Capital structure Definition

Generally, represents the relationship between debt and equity.
" Capital structure of a company refers to the composition or make-up of its capitalization and it includes all long-term capital resources via: loans, reserves, shares and bonds."Capital structure includes only long term debt and total stockholder investment.
The capital structure of a firm is the mix of different securities issued by the firm to finance its operations.
Securities
Bonds, bank loans
Ordinary shares (common stock), Preference shares (preferred stock)
Hybrids, e.g. warrants, convertible bonds

Capital Structure = Long Term Debt + Preferred Stock + Net Worth
OR
Capital Structure = Total Assets – Current Liabilities

Why Capital Structure is important :



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