THE ROLE OF CAPITAL IN THE COMPANY AND ITS TYPES

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Abstract: Every organization without regards to the products and services it produces needs capital. Capital is the driving force behind every organization, and no organization can survive without capital in the business environment. Capital is one of the necessary variables to conduct business and it's volume is determining the size of the company. Without efficient capital allocation the activity and the business dealings of the company will certainly stop. With efficient capital management has profound effect on the financial results of the company. There are two types of capital, fixed assets and working capital.

The fixed assets are the capital which is invested in a period that lasts more than a year. These assets are having three forms: material investments, immaterial investments and long term financial investments. The basic characteristic of the fixed assets is that they are not spent at once and they do not transfer their value to the finished products and services. Their costs are seen through the amortization phenomenon.

Working capital is the capital that are invested for a period of less than a year. They are also called circular assets. They constantly regenerating. They come in three types: money, materials and claims.

Capital is the basic ingredient for success of every company. It shows us that without it the companies would not be able to make purchases and make partnerships. Capital is the basic source of every business and has the power to transform the business and make turnarounds if the situation is bad, but also to worsen the situation if there is a lack of capital.

Capital can transform economies, but also could destroy economies. That is the reason the monetary policy is loose at some moments, because the lack of capital can ruin a decent economy. Companies know this and they try to capitalize themselves very well, because at times capital can be very scarce.

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1. CIRCULATION OF CAPITAL IN THE COMPANY

During the years of the business expansion the capital is circulating faster and changes forms every moment. The number of forms and the velocity of circulation of capital across those forms are conditioned by the characteristics and the activities it makes. But every part of capital doesn't have to go through those forms in the unified direction. From the number of forms through which parts of capital pass, depends the length of time passed in each form and the number of cycles.

Because these processes are complex the directions of capital in the company can be very complex, which makes tracking very hard. Because of the circular nature of capital, we can take every form as the beginning and every form as end of the capital cycle. But we should not forget that the main objective for the company is to make profit, and it is derived when we calculate the difference between the income and the expenditures, there is justification in economic theory to make money the starting and ending point, with whom the period of paying off expenditures and collecting all the income.

Subjects that plan to promote some business activity have to own some amount of capital. One part of that capital is from their own sources, but the other part can be brought from banking loans or financial institution loans, securitization of debt etc...

The making of conditions for work demands having land, building a plant, equipment and working materials.

With the collected capital the company buys fixed assets, materials etc... The fixed assets are spent over a long period of time. Their physical amortization is slow, long-term, depends on the nature of the asset, the regimen of using etc... The production process should not be understood as a way of destroying material resources, but the process of transformation of one resource into another. The result of that process are not the products that are intended for the market. The value of the products are based on the finished products. After the production process they are stored at the warehouse.

With the sale of the finished products the supply is lowered and the company is increasing its claims for the customers, and when these claims are met, it collects money from the customers. But there are processes that can appear before these phase. In a lot of cases the company may get an advance payment from the customers and the company gets monetary inflow before the products leave the warehouse. This monetary inflow causes an increase in the assets and the sources of capital in the company. After the finished shipment of the products the obligation towards the customer for the received advance payment ceases to exist and the supply of the finished products drops.
One of the main rules for capital management is that the invested assets must not lower and if there is a possibility it is good to increase them. For the implementation of this rule it is advisable that the spent amount of money to buy materials is collected by the sales to customers. For that reason the invested assets in the unfinished products and finished products are having double nature: they are parts of the overall invested assets and spent assets - costs, which must be regenerated by the income from the sales of finished products in order to keep the capital volume.

The circulation of assets is followed by their transformation and there are some changes in the volume of capital. These changes are caused by:
- Increase or decrease on the invested assets from borrowed sources of capital
- Having larger or smaller income than expenditures

Either way are met very frequently and having greater income than expenditures is the basic economic law of the company.

2. RULES FOR CAPITAL MANAGEMENT
Capital is the same as every other product of the human efforts. It has value and therefore the needed attention must be encouraged. It is different from the products for personal care, because their physical use erases their value, the products that are used as capital have a permanent role and their changes are only form changes.

The main difference between their use and the relationship between capital and products for personal care is that there are different laws for their use. Capital management abides by certain rules and principles if we are willing to succeed in our craft.

We can conclude that there is a distinction between the terms sources of assets and sources of capital. The sources of capital are showing us the changes in the elements of the passive side of the balance sheet, and the term sources of assets are affecting not only the passive side of the balance sheet, but also the active side.

The sources of capital for a company can be divided by the following systematization of Source of capital, timeframe of the capital and the costs of capital.

According to the source of capital we can have: own sources of capital, borrowed sources of capital and specific sources of capital. The own sources of capital are self-financed, borrowed sources of capital are loans and the specific sources of capital are largely donations and help. According to the timeframe we can have permanent financing, long term financing and short term financing.

Every firm prefers long term financing because it is more balanced towards the monthly payments, which are manageable and do not cause the company to come up with sources immediately. We have seen the problems at the Croatian giant Agrokor cause by overleveraging, but the real footprint of the story is that a lot of the used loans were short-term loans.

As Warren Buffet said, „When you combine leverage and ignorance, you get pretty interesting results”.

This can be used to describe the situation since the people that were responsible for risk management avoided to see the situation more clearly.

Here we must add that even the successful companies often rely on borrowed capital. But sometimes the reliance on credit becomes a burden for the company because it derives financial instability. Using borrowed capital has some advantages before the own capital that is formed through IPO, especially special rights stocks. The person or the entity that gives the loans does not manage the organization. It is only interested in the retrieval of the loan. On the other side the stock owners are interested in the management of the organization and are more centered on the work of the management.

That is one of the reasons companies rarely issue stocks and don’t want to loose control. They become more and more reliant on borrowed capital and become trapped in a bad position sometimes. That was the case with the legendary Croatian company Agrokor. After decades of successful work and numerous acquisitions, it failed the previous year. One of the reasons was overleveraging and the slowing down of the Croatian economy, but the other reasons included, reliance on loans, short-term borrowing, issuing of bonds with bad conditions for the company, mistrust from the banks, bad management etc...

A lot of existing shareholders want to to remain in power, so they force the CEO to avoid issuing stocks and instead focus on borrowing funds to lead growth and expansion. But we know from the financial crisis of
2008 that even companies like GE that produce a lot of useful products can be trapped in a bad financial position. Over-reliance on borrowed capital sources can lead to a crisis in even a good company with stealth brands.

Therefore the sources of capital are one of the most accurate predictors of corporate health, because the more we see borrowing and accelerated expansion, the more we can see the danger signs about the health of an entity. The health of a financial entity can be severely damaged if the company relies on borrowing more than it increases its capital.

There should be a difference between the velocity of the borrowing and the velocity of the capital increases. For example if the capital increases by 10%, the borrowings may increase for 1% if the company is managed conservatively. But by today’s standards these rates of increase are very unpopular and can affect the position of the company in the markets.

Unfortunately a lot of companies are forced to increase their debt to a worrisome level largely because of the following factors:
- They must keep a pace with the competition
- Competition borrows and opens new facilities and shops
- There are a lot of „cheap” loans
- There is a lot of competition in the finance sector also with the newest fintech companies, so the banks are trying to keep the pace and make their loans cheaply
- The programs for Quantitative easing were too lengthy resulting in oversupply of funds and if the company chooses not to expand, the competition would take over because it can fund itself with these sources.

The structure of capital of one company is comprised of the different sources of capital. The different classifications of the sources of capital let us look at capital from different angles. The structure of the capital can be seen from the aspect of permanent, long-term and short-term sources, own capital, borrowed capital and specific sources of capital.

The structure of capital is one of the essential signs of the financial position of the company. The interest of the company for the structure of capital is caused by the vitality of capital to affect the efficiency and the stability of the company. It affects important factors like liquidity, the business risk and the solvency risk.

A lot of companies ignore these signs, but it can lead to their demise, since undercapitalization is one of the most important factors in corporate bankruptcy. The type of products and services the company produces affects the types of assets the company needs. For every business sector there is a metric that measures the relationship between fixed assets and working capital. The structure of the assets of the company affects the structure of the sources of capital that it uses for financing.

The companies that have relatively high percent of fixed assets are more promising and therefore they almost always get financing which is long term based. We can see that if a company finds itself in tough position the first assets that disappear are liquid assets (money, products supply etc...), and the part with fixed assets is mostly stable. Therefore the amount of fixed assets is the place where the investor is looking for when he demands payment. This leads to greater overall leverage at companies that own more fixed assets than working capital.

The functional characteristics of the company are affecting the capital gains, stability and business risk. They all affect the capital structure.

Companies that work with low levels of gains are more instable and have higher business risk, on average their owners use their own money to finance them and a little amount of short-term debt.

4. FINANCIAL MARKETS AND THEIR RULE IN THE CAPITAL STRUCTURE

The financial markets influence the company's capital structure, especially by influencing the demand and supply of capital and the price of capital. The lower interest rates of the capital, which are caused by the larger capital supply are influencing bigger use of borrowed capital on long-term or short-term.

The rise of interest rates has limiting effect on the level of leverage and it enforces stricter leverage controls and investing from own capital sources.

When companies choose the sources of capital, one of the deciding factor is always the price of capital. The larger the price, the lower the demand. The widely accepted rule is that the capital structure must have quantitative and qualitative aspects that are chosen by the management.

This is brought by the following concepts:
- Companies must choose the cheapest capital
- Companies must control their debt levels
- Companies must focus on growth and innovation
- The markets are changing
- The companies must follow the competition.
CONCLUSION
The process of capital organization in a company depends on the size of the organization, volume of trading work, availability of experts etc... The financial sector of every company is one of the central organs that governs the work of the companies.

The financial bodies of the companies (mainly in middle and big companies) or the management in the small companies are the following:
- Ensuring capitalization
- Rational capital management and finding the best ways to invest capital
- Finding balance between capital inflows and outflows
- Ensuring liquidity
- Regulation of the financial relationships in the company
- Success in the financial market dealings
- Positive financial result
- Financial planning
- Financial analysis

The capital in the company is the main force in the business dealings. It is used for some of the business tasks.

One of the most important moments in the business is the source of capital, the structure of payments and the guarantees that are used to obtain capital. But the sources of capital are often influencing the ways capital is invested in the companies. It is because of the timeframe, costs of capital etc...

A lot of times the companies must find a way to find a balance between the capital and the investments the company makes and the sources of capital.

Investments of capital are causing expenditures. In order to decrease the expenditures it is important to have higher circulation of capital and higher turnover.

In the task of ensuring liquidity the company must manage the capital inflows and the capital outflows. The company as an organization has contacts with internal and external subjects.

There are a couple of ways the companies can manage their assets more effectively: measure debt, increase their profitability, gain monetary reserves, insure their risk, decrease their dependence on borrowed funds etc..

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