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A Bibliometric Analysis on Capital Structure of SMEs

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ABSTRACT

The capital structure of an organization is the outcome of financial decision taken by firm. The capital structure is highly affected by market conditions and other external factors. SMEs are gaining interest in various research studies due to their distinctive organizational features and benefits. The present study will explore key areas, contributors and key dynamics of capital structure in context with SMEs. This study will adopt bibliometric analysis with the help of reviewing various research studies from competitive journals and research articles. The articles will be divided as per the theories such as pecking order theory, agency theory and trade-off theory. Determinants of capital structure, trade credit, corporate governance, and bankruptcy are also the prominent research topics in this field. Also, this study will identified the research gaps and recommend actionable research directions for the future.

1. Introduction

Capital structure is known as a schematic which is used by an organisation to design the expenses. The capital structure is one of the most important things that a company focuses on as it will determine how much profit they will have and how much they have to spend. Capital structure consists of two parts (Mac and Lucey 2010).

- Financial assets in which a company analyses all the financial assets that they have and focuses on the assets that they are about to make or buy.
- Debt and equity in which the company analyses the liabilities and the equity of the company. There is a term given to this analysis known as Hybrid Security.

Both debt and equity of a company is maintained in the company’s balance sheet. This balance sheet contains long term and short term debt, common and preferred stock. The capital structure of a company is determined by comparing the long term and the short term debt. A company which has more debt than equity has a higher leverage ratio and an aggressive capital structure. Similarly, if a company has more equity than debt then the company has a lower leverage ratio and a conservative capital structure (Kenourgious et al.2020). The capital structure of small and medium size firms is significant and an interesting topic of research among various studies due to the role of SMEs in economic development. SMEs enhances the employment opportunities in a particular economy by contributing to GDP and social progress. There are significant externalities related to SMEs such as improvement in quality of education through economic development and social progress, overall increment in human capital, better living and increment in gross domestic product. In developing countries, SMEs are known as engine of growth and development. Hence, it is significant to understand the concept of capital structure in SMEs for future recommendations for growth and development (Savvakis et al.2020).

2. Distinctive features of SMEs

SMEs are the small and medium sized enterprises that are no subsidiary and independent organizations. These firms do not accommodate as many people as a higher organization and therefore we can say that the accommodation capacity is below average in comparison with higher organizations. The highest accommodation capacity ever seen was 250 people. However, there are other SMEs which have a capacity limit of 200 employees. There is a term called ‘Micro enterprises’ which is said to have the maximum employee capacity of 10 people and some of them have fewer than 10 people (Gelinas and Bigras 2004). These SMEs are one of the elements that contribute to a country's economy. According to many surveys, it is seen that SMEs are considered to be the backbone of Australia. It provided around 6 million jobs in Australia and contributed around 60% of Australia's GDP. This contribution of the SMEs in a country's economy is divided into five main parts.

- Employment creation in which these SMEs provide new job facilities for the people who are unable to find a suitable job.
- Adaptation and flexibility which allowed the people to work according to their comfort ability.
- The availability of SMEs paved a way for entrepreneurship as people were encouraged to start their own business.
- SMEs have provided the facility to work in as a sub-industry in large enterprises.

All the above mentioned points paved a way for the SMEs to contribute their part in a country's economy. The main point among these is employment creation. The employment creation sector is the direct link between a country's economy and a country's growth. There are numerous cities which are affected by the establishment of SMEs as their economy has shown a good improvement. Some of these cities are Istanbul which showed an improvement of 28%, Bursa with 7%, and Antalya with 8% (Ograca, 2010).

It is very much clear that SMEs have a distinctive role in society and have a good contribution in the economy of a country. Therefore, to understand the SMEs better, the features of SMEs must be kept in mind (Jafari et al. 2007).

More People Friendly

SMEs are small or medium sized enterprises with a very limited number of employees. These enterprises are directly linked with the people as they are the ones who are finding and providing employment to the people. Moreover, being a smaller company means that they are more focused on getting their work done and in many cases it is seen that these enterprises are more customer and people friendly as they have the tendency to help their employees (Jafari et al. 2007).

Ability to Adapt

The major advantage of the SMEs is their adaptability. They can be flexible and can change themselves according to the market trend. This is because these SMEs are linked directly to the people. The interaction between the enterprise and people is more than bigger enterprises. Through this interaction, the market trends and the demands which people are having can be understood better by the SMEs. Moreover, through this interaction, the SMEs can design their capital structure and can invest on a particular project accordingly (Ogarca, 2007). They can also decide the importance of a particular project and can stop the production of a particular project if that product is no longer demanded by the people (Al-Najjar, 2018).

Employee engagement

The SMEs mainly work in rural areas and tend to provide employment to the people who are not able to find work for themselves. These SMEs have a very low employee capacity and work within a small corporate circle. Therefore, the smaller the corporate circle, the better will the people know each other. This statement can be understood as; people who are working in a big enterprise have numerous different departments (Al-Najjar, 2018). These departments only come together when they are assigned a common task. However, in case of SMEs, the number of departments is low and people who are working in these SMEs have to work together in terms of production. Therefore, they have a better chance to know each other.

Effective decision making

In large companies, if a product is to be made, it has to go through numerous authorities and the decision is not taken by a single person but goes through meetings and group talks. The people who are indulged in this decision making are not doing it alone. This practice makes the decision making process time consuming (Claudia et al. 2013).

However, in SMEs, the decision making mainly falls into the hand of a single person or a small group. This phenomenon reduces the decision making time and makes it more swift and efficient. Moreover, if a single person is given the responsibility of taking decisions regarding different matters of an organization, the decision making power that person will automatically enhance.

3. How do SMEs finance themselves

Whether the enterprise is a small or medium size enterprise. The main thing to run the company is financial support. Every company requires a stable form of investment as this investment will ensure that the conditions and the standards are maintained in terms of production and company maintenance. To meet these financial demands, the SMEs are now focusing on investing in external funds and are considering raising these external funds for expanding their businesses (Khan, 2015).

A corporate head or a company owner knows that to make a company successful, they have to get a stable financial inflow and this can only be met if they have a good investor. They understand that making and selling the product cannot satisfy a long term profit plan. Therefore, to have financial stability for the company, an investor is very much important. Sometimes, the SMEs go for private investors in which the investors invest their own money in the company and take a small amount of the profit which the company makes by selling their products. However, there are small SMEs which opt for government help and apply for loans provided by the government for business purposes and utilize that money to build the business and repay the loan on the given time. Therefore, this is understood that there are numerous options for SMEs to have investors; however, there are some common funding opportunities for all the firms (Abbasi and Abbasi 2017).

Retained Earnings

A businessman thinks to make a company which will make good and innovative products that will help that company to grow in the market. The primary objective of a businessman to make products and sell those products to make profits. Though these profits are not that much, the primary thinking of all business owners is the same. Therefore, the amount left from the profit after all the expenses and obligations are called Retained earnings. These earnings are used by the business owners as a form of investment which they use to grow and expand their business. Moreover, the retained earnings is a very stable form of profit generation (Jiang and Lin 2014).

Debt Capital

Companies or the business holders who are not able to invest a good amount of money or do not have the money which is required for the business have the option to borrow money from the market. This phenomenon of borrowing money is known as the debt capital. Companies can borrow money through private investors or by opting for bank loans (Baker and Kumar 2020). The investors or the loan providers give a date on which the lender has to return the money. If the lender fails to return the money on the given time period then the lender falls into bankruptcy or default category. This borrowing and lending money is done under corporate bonds which enables the investors to become potential money lenders for the company (Kumar and Rao 2015).

Equity Capital

If a company fails to have a potential investor for them, it can sell their shares to the stockholders to raise the money. The stockholders buy the company shares in a very good amount providing the company has a good amount of money which they can invest in the company. Moreover, the stockholders who are buying the shares of a company need not have to pay interests like the bondholders do (Kumar and Rao 2015).

4. Factors affecting the capital decisions of SMEs

Sales Stability

A capital decision or capital structure is made by a company to determine the expenses and the profits that they are having by selling a product. This structure helps a company to make a schematic framework of the work that they have to do and the procedures which they have to adapt to reduce the expenses and increase the profits. However, all these schematics and processes are purely based on the sales (Dvorsky,et al. 2019). If the sales are not that efficient then the capital structure or the capital decision can get affected. Therefore, it is very much important to have a stable sale as the stability will ensure that the company which you are owning will have a good capital structure.

Financial Flexibility

A SME whether it is small or medium has to be flexible. It must have the capability to understand the demands of the people and must follow the market trends before introducing a product in the market. Companies which are not flexible can see a drastic fall in their sales graph (Wallis, 2006). This is because, when a company makes a product, they make it for the people. The people will have certain expectations with the company which, if not fulfilled, will make the company suffer. Therefore, it is very much important for a company to become financially flexible so that it can sell its product successfully.

Cost of Capital Floating

Every company has a desire to make more and more profits. The company owners opt for different investors who invest in the company and make the company more efficient. Some companies have more than one investors who are investing in a company. In the case of SMEs, only a handful of them are having more than one investor. However, the ones that are having more than one investor must be careful while opting for an investor. They must understand which one is cheapest and most importantly they must know what the alternative is if an investor refuses to invest in a company (Khan,2015).

Market Conditions

As discussed previously, it is very much important to understand the market trends before making a product. In this era, the market is very unpredictable and people who will be taking your products will always demand more. However, you must understand what is suitable for you and must decide how to make a product with less investment and make more profit. However, you must also look for the quality of the product (Hussain et al. 2006).

Period of Financing

Companies tend to have eternal investors for the company's growth and efficiency. This form of investment is known as equity capital. This capital is more than the ones which they can make by making a product. However, this capital is a time bound one and has to be repaid in a given time which if not given can result in bankruptcy.

5. Literature review

Palacin et al. (2013) studied the capital structure of SMEs in Spain. This article inspects whether the capital structure of SMEs and its firm-factor determinants are unique across areas having a place with a solitary country. This subject is moderately imaginative in capital design research, since most of the examinations did in a solitary nation have fail to consider the locale wherein firms work to clarify influence. This study explored whether the capital structure and its firm-factor determinants—size, resource structure, benefit, development, and age—vary contingent upon the district in which the SMEs are found. For the experimental investigation, board information strategies are applied to selected firms from all areas of Spain for the period 2004–2007. The results of the study not just propose that there are provincial contrasts in the SMEs capital structure yet in addition affirm that the effect of firm factor determinants on influence contrasts across areas as far as signs, extents and importance levels.

Abor and Biekpe (2009) studied the capital structure of SMEs in sub-Saharan Africa. This study investigated various factors affecting capital decisions in small and medium sized enterprises in Ghana. This study is regarded as significant due to immense importance of small and medium enterprises in increasing the growth and development of Ghana's economy. The study made an attempt to analyse the firm level characteristics and its impact on short and long term debt ratio. For this relationship analysis, this study utilized regression model. The results of the study claimed that various firm level characteristics such as growth of firm, size of firm, extent of profitability and assets of the firm significantly impacts the capital structure. The study concluded that short term debt is significant source of finance among Ghanaian SMEs. This study is highly useful for government, policy makers and entrepreneurs of Ghana.

Cassar and Holmes (2003) explores the determinants of capital design and utilization of financing for SMEs of Australia. Speculations using static trade-off and hierarchy contentions are experimentally inspected utilizing a progression of firm attributes including: size, resource structure, productivity, development and danger. The theories created are tried utilizing an enormous Australian cross country board overview. The outcomes propose that resource design, benefit and development are significant determinants of capital construction and financing. For resource structure the heading of the impact is dependent upon the capital construction or financing measure utilized. The outcomes by and large help static trade-off and hierarchy contentions proposed by hypothetical models.

DiPierto et al (2017) linked the regional development and SMEs. This article considers the impact of provincial institutional climate, estimated as territorial turn of events, on capital decisions making of SMEs. Besides, the standard firm-factor determinants and the business area of the firm are likewise fused. To this end, a sample of 6,560 Spanish firms for 2007 is investigated, where all areas of Spain and all areas, aside from the monetary area, are thought of. Spain gives a reasonable and neglected research facility for the investigation of territorial contrasts in the monetary design of SMEs, since, from one perspective, SMEs comprise the most pertinent firms in this country, and then again, Spain shows local inconsistencies at different levels. Also, the observational examination utilizes Partial Least Squares (PLS), a fluctuation based underlying condition demonstrating (SEM). In this regard, PLS has a few clear benefits to different direct relapse (MLR). Because of this investigation, how every one of these variables clarifies the variety in the capital construction could be appeared. In addition, the outcomes show that albeit firm factors and the business area clarify a huge extent of the fluctuation of capital design of SMEs, it is imperative to consider the provincial institutional climate to more readily determine the degree of obligation of SMEs in a solitary country.

Farouk et al. (2017) explored the capital structure of SMEs in UAE. The motivation behind this examination is to recognize the capital design choices and the institutional elements in female possessed SMEs in the United Arab Emirates. A study poll technique was utilized to gather information from the neighbourhood female business visionaries, and a factor examination was directed to comprehend the capital design choices and the institutional components influencing SMEs achievement and activities. The discoveries uncovered that most of the Emirati female business visionaries favour interior (own reserve funds, advances from loved ones for business start-up) instead of outside financing sources. UAE State Bank and global loaning organizations were other famous decisions for sourcing advances. They consider factors like faculty, capital, preparing, government, and brand notoriety will influence the accomplishment of their organizations. Nonetheless, the board abilities and client assistance factor appears to overwhelm. The serious issue that the Emirati ladies business visionaries looked in acting naturally utilized are endeavours to oversee, for example, a lot work, duty, and no an ideal opportunity for family. Business area, stopping, attention to procedural changes, and absence of clearness in strategies were the predominant institutional components that influence their business activities in the UAE. The investigation will help the arrangement creators in recognizing the particular pioneering factors which will lead in planning powerful and pragmatic strategy intercessions nearby capital construction and expertise working of female Emirati business people. The quantitative examination give new and current bits of knowledge into the different issues influencing ladies business people from a country that is endeavouring hard to enable its females.

Golic (2014) studied the crowd funding as a significant method of financing among SMEs. The absence of financing, and restricted admittance to it are the fundamental issues looked by SMEs. Given the incredible job and significance of SMEs in each public economy, any advancement in taking care of these issues regarding making and discovering elective wellsprings of financing ought to pull in extraordinary consideration in both expert and logical and the more extensive socio-political networks. Crowd funding is an inventive and moderately new idea that associates business people and financial backers through the Internet. This technique permits the business visionaries to gather assets through the Internet by "open greeting" to back their activities/adventures and hence raise the vital assets by moderately little commitments of a generally enormous number of financial backers. Accordingly, crowd funding is a quickly developing model progressively bantered of in scholastic circles and the European establishments. This paper considered crowd funding as an elective methods for financing SMEs and attempt to give various parts of crowd funding - and clarified how it functions, what are the upsides of utilizing it for SMEs and accordingly grow the information on the subject.

Baker et al. (2020) studied various preferences of financing sources of SMEs in India. Utilizing review information from 309 SMEs from the northwest India, this examination inspects the financing inclinations and practices of these SMEs. It likewise explores the distinctions in the financing inclinations across firm and proprietor/supervisor attributes and records the drivers of financing rehearses in India. Respondents lean toward interior assets followed by bank financing for the most part as long haul advances and assets from government and monetary establishments. Among casual sources, SMEs favour exchange credit followed by assets from family companions, family members, and cash moneylenders. The most un-favoured wellspring of financing is outside value. The investigation adds to the surviving writing on SME financing by contrasting the financing inclinations and practices of SMEs and distinguishing a financing hole. By giving an all-encompassing perspective on financing sources to SME proprietors and supervisors, the examination can help policymakers in planning proper strategies for these people and help recognize underutilized financing hotspots for SMEs.

Abbasi et al. (2017) explored the role of government in developing SMEs. There is no doubt that financing is a critical apparatus for the development of any firm and getting to the correct kind of financing as per the company's need is of more indispensable significance. Admittance to back for Small and medium firms (SMEs) is consistently a debated conversation for the analysts. Having realized that SMEs are considered as spine of economy and assume key part for the development and improvement of country, they face obstacles while getting to the account from monetary organizations. Keeping in see the significance of SMEs, this paper plans to enlarge the comprehension on the accessible elective financing alternatives available to SMEs also, business visionaries; this will improve their insight about the full extent of financing instruments that they can access in different conditions and by having sound conversation among partners about new techniques and imaginative procedures for SME and business endeavour financing. Other than that, this paper additionally expects to features the SME socioeconomics and job of government for supporting the SMEs.

As per Kraja et al. (2014) Government policies have incredible effect on financial advancement of any country. SMEs are extraordinary source of monetary turn of events, pay age and occupation creation in an economy. Government strategies are key components that influences the achievement and execution of SMEs. Along these lines, it is fundamental that organization ought to backing and start such activities for SMEs, with the objective that ought to have an economical improvement of the economy. For the most part governments are resolved and centred to help the SME business, to have a consistent economy. Governments are by and large quick to help the SMEs from that degree where they cannot create reserves for their productive tasks, also governments are keen on supporting inventive endeavours, which is one region where SMEs for the most part surpass assumptions, and furthermore quick to help the SMEs development because of their work creation. As of late, with the help of government projects for SMEs in numerous nations, it has ended up being dynamically possible to offer such combination of devices to SMEs having low credit scores and inconsequential financing needs than what may be in real in private capital business sectors.

As per Appiah et al. (2019) the significance of SMEs, governments and worldwide SME uphold affiliations principally intercede through: I) inclusion in the business market with speculation finances that honour orders to private endeavours masters; ii) direct open financing to SMEs under projects administered by open monetary foundations; iii) assurances to private foundations that offer financing to SMEs; iv) sponsoring of private financing associations at extremely appealing terms. These mediations by governments for help, profiting the SMEs at bigger scope. The benefits incorporate; - loosened up financing requirements, improving admittance to fund; - helping SMEs to become further by arrangement of awards and master advices; - offering wide scope of financing items to SMEs and business people; making it adaptable to lead business in open area; - helping SMEs through charge unwinding; - SMEs without security may look for government's help; - and by ensuring the credit and giving value venture

6. Objectives of the study

- To investigate relation between size of firm and debt level in SMEs
- To measure the relationship between Short term debt and growth opportunities in SMEs
- To understand the significance of Leverage and profitability of SMEs

7. Research methodology

The present study is based on extensive literature review. The objectives of the study are achieved through reviewing past research insights related to present context. This study is based on secondary data analysis. The prominent research articles from various journals of management and industrial research are utilized in this study.

8. Results and discussion

There are various views regarding the size of firm and debt level in SMEs. Modigliani and Miller (1958) claimed that debt level of a firm are related with market efficiency and models adopted in a particular business, there is no relation between size of firm and level of debts. Apart from this, there are studies debating about the positive and negative relationship between debt level and size of firms. Heshmati (2001) expressed that corporate sector is reported to have easy access to equity capital as compared to small firms due to low fixed costs. Hence, it is claimed that there is a negative relationship between firm size and level of debts. Other authors such as Fama and Jensen (1983) explained that the transaction costs and asymmetric information issues are not available in large firms while small and medium size firms are features with lack of information and high transaction costs. Therefore small and medium, size forms raise funds from debts rather than equity. The probability of bankruptcy in small firms is more as compared to large firms. Singh and Hamid (1992) explained there reasons behind the positive relationship between firm size and level of debt. Firstly, it is claimed to be a strong association between size of form and risk of solvency where small firms are more prone to solvency risk. Secondly, transaction costs are higher in small firms and thirdly, lack of symmetric information in small firms. Hence it is accepted that there is a positive linkage between debt level and size of firm in SMEs.

There is positive relation between size of firm and debt level in SMEs

As per Meyer (1977) debt financing provides growth opportunities to a firm but it could arise agency problems such as conflicts among shareholders and bondholders. Agency issue can be resolved by considering short term debts in SMEs rather than long term debts. Hall et al. (2004) contemplated that growth opportunities are possible with sort term debts since companies can borrow more capital for further investment. Short term debts decreases agency cost and transaction costs in SMEs. Hence, short term debt is reported to be positively related with growth opportunities in SMEs.

Short term debt is positively related with growth opportunities in SMEs

It is contemplated in various studies that SMEs are more inclined towards utilizing internal funds rather than external funds. As per Meyer (1984) when SMEs generate acceptable amount of earnings and profitability within the firms, then there is a less possibility of leverage. This conclusion is drawn from pecking order theory. Petit and Singer (1985) explained that small and medium sized firm’s finance capital in a hierarchal manner. Due to the non-availability of symmetric information as maintaining audits in SMEs are costly, firms are reluctant to provide financial information. So, the option of equity is complex. The issue of asymmetry and cost of credit highly influence the level of leverage in small and medium size enterprises. Furthermore, the hierarchal order of source of financing among SMES is retained earnings, debt and equity. When the level of profitability is more in SMEs, the extent of leverage will be lower.

Leverage and profitability of SMEs are negatively related with each other

9. Conclusion

This research article is based on evaluating the capital structure of small and medium size enterprisers through a detailed review of literature. From the above analysis, it is concluded that SMEs are significant for economic growth and development of a nation. SMEs helps to provide job opportunities and employment in a particular nation by adding up human capital. The capital structure of SMEs and large companies are significantly different from each other due to availability of various factors. There are various determinants of capital structure of SMEs which directly impact the capital decisions making in SMEs such as size of firm, life of firm, nature of firm, profitability, assets structure and availability of operational risks. It is concluded that SMEs prefer internal funds for financing rather than utilizing external funds. Furthermore, short term debts are beneficial for SMEs rather than long term debts. Crowd funding is reported to be popular source of finance among SMEs currently.

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