

A Study on the Relationship between Outsource Financing Processes and Companies' Performance

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Abstract: Today, financial resources financing is among the most important economic concerns and responsibilities. Companies can use different methods to finance. Currently, financing methods are effective on continuance of operations and implementation of profitable projects, in the companies' growth process, and lead to the survival of companies in today's competitive world. The current study aimed at investigation of the relationship between outsource financing methods and companies' performance. In this regard, the two variables namely the bank loans and capital increase were considered. The statistical population of the study included the companies listed in Tehran Stock Exchange, in a 5-year period from 2012 to 2017. The results of the study showed that there is a significant relationship between the company's performance and financing through the capital increase. Also, about the financing through bank loan, it was revealed that there is no significant relationships between the company's performance and this method of financing.

Keywords: Financing, Capital, Bank Loan.

Date of Submission: 14-04-2018

Date of acceptance: 02-05-2018

I. INTRODUCTION

Today, the companies can finance through different methods. The financial managers' awareness of different financing methods and means, and their effects on the enterprises, lead to the continuance of the enterprises activities, and makes their financial structure less vulnerable, as well as facilitating the operations flow. The correct perception of the effects and relationships of financing and operational performance helps the managers with their strategic and fundamental decision-making, and provides those who are interested in investing in these companies, with proper information.

Generally, the need to finance is felt due to: firstly, the companies' capital value is decreased as a result of external factors such as the exchange rate, inflation, bank interest rate. Secondly, the companies operational processes lead to the need for financial resources in the form of finance, in order to purchase new assets, increase plant capacity, hire new forces, and buy raw materials [1]. In this regard, the proper obtaining of the resources would lead to the company's success in the market, and the companies can follow the market opportunities through this method, and enjoy the advantages of working in the market [2]. Since the economic organizations and institutions are highly dependent on the financial markets for financing their capital, these markets play an important role in provision of the capital needed for the organizations. In fact, the capital market provides the organizations with the possibility of financing their financial resources through the investments. In other words, the capital market acts as a path for transference of resources from the financial resources savers to the consumers, and through provision of the capital needed by the economic institutions, and optimal allocation of the resources, plays an important role in countries' economy.

Currently, the financing methods are highly effective on the activities continuance and implementation of the profitable projects in the companies' growth process, and lead to the survival of the companies in today's competitiveworld. The financing is done in various short- and long-term methods, and the organizations can finance their financial resources, either internally (for example through accumulated earnings) or externally (through issuance of stocks or bonds). The main goal of any organization is to increase the Return on Equity (ROE), and to this purpose, they use methods that help them with this goal. The increase in ROE and the consequent decrease in cost of capital, leads to the increase in company's value. In fact, the investors,

including shareholders or lenders, and long-term lenders, by granting their capital or money to a company, have accepted the risk of non-compliance, and will seek a return equal to the company's cost of capital [3]. The question raised in the current study is that whether these financing methods are effective on the company's performance or not?

II. FINANCING

Financing is among the matters raised in discussion of launching any new investment. The financial capital is the capital held by the banks, which is used by the owners of the industry. Financing is the art and science of cash management. The goal of financing is investing, profitability, reducing the risk, and meeting the company's economic and social needs. Profit acquired from business is considered as one of the important factors in the continuation of business activity and is an important source of funding the operating activities of the firm in the future. Among the concerns of the economic enterprises in the world is the provision of desirable finances. Any kind of activity requires financial resources. Thus, the financial resources are likened to the vital artery of business and small and large enterprises. In fact, the main purpose of any kind of economic activity is profitability, and it is not possible without the availability of financial resources [4].

2-1- Financing Methods

The organizational financing methods include the followings:

- 1- Internal Resources (other resources): Internal resources are revenues from the provision of services or the sale of goods and other activities that state-owned companies are permitted to do under the laws and regulations, and they ultimately lead to the annual profitability of corporations. Other resources of financing include the amounts under the title of the loan, the issuance of bonds, the return of previous years, and similar titles that are predicted in the budget law of the country, and do not have the nature of income.
- 2- Public Revenues: Public revenues include revenues from government ministries and institutions, taxes, dividends from state-owned companies, and revenues from monopoly and ownership, and other revenues that are included in the general budget law of the state as general income. Since public revenues are essentially government-owned and are collected by nine state-owned organizations, there is no direct relationship between its collection and consumption.
- 3- Bank Loans: a part of the funds listed in the annual resources of the companies' annual budget is called bank loans, which is received to cover a part of the projects construction costs.
- 4- Buyback Contract: the buyback contracts are among the severance contracts. In this type of contract, the foreign investor company pays all investment funds, as well as the costs of installation of equipment and technology transfer, and after the project commissioning, it is transferred to the host country. Return on investment as well as capital gains are obtained through sale of products. This type of contract is used in countries where their laws ban any private or foreign ownership of the industry.
- 5- Finance: Financing means that a bank or foreign business entity lends money to a country or a certain company for a specific operation, and actually, it does not have any control over its expenditure, and therefore, there is no obligation upon it for the plan efficacy, and it receives the original contract and interest of the lent money in certain periods, from the contractor or the bank guaranteeing the contract.

2-2- The Main Reasons of the Companies Financing

Generally, the intentions of the managers for financing can be mentioned as three main reasons: Repayment of debt, investing in new projects, and counterbalancing the shortage of operational cash flows [5].

- 1- Repayment of the Debt: Debt means the financial rights of individuals (other than the owner) to assets of an economic unit. Debts represent the financial liabilities of an institution in terms of the assets or credit services received from others, created in the past and present, and they will be repaid by transference of assets or provision of services in the future. According to the above definition, it can be understood that debts are usually made in exchange for the acquisition of assets or the use of the services of others that have been done in credit, and they are registered in the offices when the amount and time of repayment are agreed upon by the contract parties, and the commitment to pay is confirmed by the firm [6].

Dent separation in terms of time of repayment, is so important, since the enterprises managers and owners try to timely pay their debt with awareness of the time of repayment, so that they do not lose their reputation and trading position to other institutions and sellers, and in the future they can also use their credit facilities and loans in a desirable manner. The debts are divided into current and short-term debt, and non-current or long-term debt in terms of time of repayment, and there are debts repayable within a few years. These types of debt are of particular importance in the financing and capital structure of the company. Repayment of debt usually involves repayment of the original debt and repayment of its interest. The debts are usually repaid in certain periods of time [7].

2- Investment in New Projects: according to most experts, there is a definite and unavoidable relationship between the growth and amount of investment, and access to first is impossible without application of the other. The optimal application of production resources is an acceptable strategy, approved by all experts, and it can be obtained through investment, confirming the importance of the investment in economic growth and development. The increase in the productive forces of the society that lead to the increase in production, economic development, total employment, and especially, the promotion of the income, would not be possible without the local and foreign investment and the use of capital in various economic activities, and it would turn into an unreachable desires. Among different types of financing, investment is one of the most effective methods. Alongside the many problems, challenges and pre-requisites that are significant for successful and effective investment attraction, designing and applying effective incentives for directing capital inflows into sectors, sub-sectors, disciplines and various economic activities are of great importance [8].

3- Counterbalancing the Shortage of Operational Cash Flows: the cash flows can affect the enterprises performance and lead to the changes in efficiency and profitability. Operating cash flows are the increase or decrease in cash amounts due to the main and continuous activities producing of the economic unit's operating income [9]. Cash flow is one of the most important sources in each economic unit, and a balance between available cash and company needs is the most important factor in the economic health of each business unit. Cash is entered into the economic unit through normal operations and other sources of financing, and it is used to execute the operations, paying profit, repaying debts, and expanding the business unit [10]. Due to the importance of cash flows to the success of business units and the need for their survival, managers use cash flow, especially the operating cash flow, in new financial analyses.

2-3- The Types of Financing Methods

In a general categorization, the methods of companies financing are divided into two categories:

- a) Short-term financing
- b) Long-term financing

Short-term financing: it is type of financing, repayable in a year. Three main sources of short-term financing are:

- Commercial credits
- Getting loans from commercial banks
- Publication of commercial papers [11].

Long-term Financing: it is a type of financing obtained through long-term sources. In other words, it is repayable in periods more than one year. The most important sources of long-term financing are:

- Issuance of bonds
- Distribution of ordinary share
- Distributing of preference share
- Financing from accumulated profits, also called inter-enterprise finance [11].

The first three sources of long-term financing and the short-term financing sources are called outsource financing, since they are provided from outside the enterprise.

2-4- Companies Performance

The concept of performance is associated with efficiency and effectiveness, since the effectiveness is indicative of the level of achievement to the goals, and efficiency indicates that how the sources are economically used for achievement to the goal. The efficiency and effectiveness can be considered as two important dimensions of performance, i.e., both internal causes (efficiency) and the external causes (effectiveness) can be present for the particular parts of performance, and therefore, performance is a function of the efficiency and effectiveness of activities. The common framework for various financing methods is usually borrowing, liquidity flows, and the use of common shares [12].

As long as the enterprises are trying to survive and require themselves to be present in the national and international levels, they must set the foundation for continuous improvement. This principle cannot be achieved unless the way for reaching it is paved by improving performance management. This improvement can be achieved by obtaining feedback from the inner and peripheral environment, and analyzing the strengths and weaknesses, and opportunities and threats, accountability, and customer satisfaction, by creating and applying an appropriate performance evaluation system. The various financing methods greatly help with the flexibility of plans, objectives, and missions of organizations in today's dynamic environment. The evaluation and measurement of performance and its development require culturalization and promotion of organizational culture [13].

III. REVIEW OF THE RELATED LITERATURE

Tongurai and Vithessonthi in a study (2015) titled "The leverage effect on the performance of native-leading companies versus internationally-managed companies", investigated the leverage effect on 159375 non-financial companies in Thailand, during the financial crisis of 2007-2009. For example, it was concluded that there is a negative relationship between the leverage effect and the firm's performance. In addition, the leverage effect on performance is negative for native-managed companies and is positive for companies with international management. Also, the size of the company modifies the leverage effect on performance. These results may be attributed to the fact that internationally-managed companies tend to have more resources, knowledge, and abilities than native-managed companies [14].

Kroes and Manikas (2014) in a study titled "Financial Management and Performance of Manufacturing Companies: A Longitudinal Perspective", with the aim of developing the previous studies, examined the relationship between changes in circulating funds criteria and financial performance of firms using examples of longitudinal data from the company. The study of changes in the specific criteria of liquidity in terms of changes in the Tobin's Q Ratio indicates a reduction in received accounts, as well as a decrease in inventory related to the improvement of financial performance of the company, which has continued over several periods. The nature of introversion also explores whether the cash management strategy of a company would lead to a change in the company's performance or whether the circulating fund strategy could be considered as a subsidiary of the firm's performance [15].

Yero (2013) examined the level and increase in leverage effect on the ability to manipulate the liquidity in Nigerian companies over the period of 2005-2010. The results indicated that there is a significant and negative relationship between the leverage effect and the ability to manipulate cash flows [16].

Mumtaz et al. (2013) concluded in a study titled "Capital Structure and Financial Performance in Pakistani companies" that the financial performance of Pakistani companies has a negative and significant relationship with their capital structure. There is also a negative and significant relationship between capital structure and market value. In addition, when the share of debt increases in the composition of capital structure, the risk level also increases [17].

Hashemi and Kashanizadeh (2012) examined the effect of leverage effect, operating cash flow and size of the company on profit-sharing policies in companies listed in Tehran Stock Exchange between 2003 and 2010. They concluded that profit-sharing policies have a negative relationship with the leverage, and a direct relationship with the operational cash flows and firm size [18].

Wayhudi (2011) dealt with the analysis of effect of cash flows on leverage and its relationship with the future performance of Indonesian companies. The results confirmed that the simultaneous entry of leverage and cash into the model results in a negative relation, that is the verification of hierarchical theory. On the contrary, by the application of a one-year timeout, this relationship becomes positive and it would be correlated with signaling theory [19].

Gordon and Lee (2010) in their study titled "Tax Effects on Financing Processes through debt in American Companies" showed that tax has a strong and significant relationship with the level of corporate debt, especially the difference between large and small corporates tax rates (34 percent versus 15 percent), and large corporations with a higher tax rate compared to smaller corporations with lower tax rate, use their debt instruments to finance themselves [20].

Covas and Wouter (2007) conducted a study titled "the role of financing through debt and share during economic fluctuations". The research findings, examining the two methods of financing showed that firstly, the financing of companies has periodic behavior and also depends on the size of the company. Secondly, the researcher provides a framework based financing through debt, in order to modify its use and move toward financing through the share, for reducing the undesirable debt effects [21].

IV. METHODOLOGY

The current study is of correlation type, and an applied research. For data collection, the specialized books and Persian and English magazines, as well as the internet-based articles have been used in a comparative-causal form. In this method, the goal is to analyze and interpret past events and information in order to discover common and shared features, and better understand events, and anticipate similar events in the future.

V. RESEARCH HYPOTHESES

Main Hypothesis: there is significant relationship between the outsource financing and companies' performance.
Sub-hypotheses:

- 1- There is a significant relationship between the capital increase methods and companies' performance.
- 2- There is a significant relationship between the bank loans and companies' performance.

VI. STATISTICAL POPULATION

The statistical population of the current study included all the companies listed in Tehran Exchange Market. These companies should have the following qualifications:

- 1- Due to the major difference in activities, they should not be among the investment and financial intermediation companies, financial institutions, and banks.
- 2- Companies' financial statements and notes are available during the period of 2012-2017.
- 3- Selected companies should be financed only by the capital increase (from cash and solvency) and bank loans.
- 4- Companies whose annual returns are not measurable due to their non-tradable stock are excluded from the statistical population.
- 5- Finally, companies that qualify for the test statistic are independently divided into two major groups in each year:

First group: Including companies that are financed through capital increase (cash and solvency). In this group, companies with a higher return rate than the average return rate of all companies listed in the Tehran Stock Exchange have a better performance. But companies whose overall returns are lower than the average return rate of all companies listed in the Tehran Stock Exchange, are inappropriate and have a low performance. In this group, 86 companies were selected according to the mentioned criteria, among which 59 companies had good performance and 27 companies had poor performance.

Second Group: including companies that have been financed through a bank loan. In this group, 258 companies were selected as the sample, among which 66 companies had good performance and 192 had a poor performance.

VII. DATA ANALYSIS PROCEDURE

For testing the main hypotheses, the Chi² (x²) statistical procedure is used due to their qualitative variables. In this hypothesis, we sought to investigate the existence of a relationship between the financing methods and companies' performance, and this method is used for evaluation of the dependence and independence of the variables. The H1 and H0 for the main and sub-hypotheses are as follows:

$$H_0 : P_1 = P_2$$

$$H_1 : P_1 \neq P_2$$

The test statistic distribution is calculated by the equation 1:

$$\chi^2 = \frac{\sum \sum (O_{ij} - e_{ij})^2}{e_{ij}} \quad (1)$$

For the first and second sub-hypotheses, the ratio test statistical procedure is used. In these hypotheses, we seek to investigate whether there is a significant relationship between the companies' performance and one of the bank loan and capital increased financing methods? The H and H hypotheses of this statistical procedure are as follows:

$$H_1 : P_1 \leq P_2$$

$$H_0 : P_1 > P_2$$

The test statistic is calculated as follows:

$$z = \frac{\hat{p} - p_0}{\sqrt{p_0(1 - p_0)/n}} \quad (2)$$

VIII. CONCLUSION:

According to the results, there is a significant correlation between financing methods and companies' performance (main hypothesis). The test was conducted for the period of 2012-2017 and the main research hypothesis has been approved for all years.

Also, the results of the first sub-hypothesis testing indicate that there is a significant relationship between companies' performance and financing method through capital increase. The findings indicate that out of the 86 companies that are financed through the capital increase method, 59 companies had good performance and 27 companies has an inappropriate performance, and this difference is not statistically significant. The value obtained for Z is 2.86, and this value lies in H0 rejection domain and rejects the H0 hypothesis.

On the other hand, the results of testing the second sub-hypothesis indicate that there is not a significant relationship between companies' performance and financing through a bank loan. Accordingly, from the 258 companies financed through the bank loan, 66 companies had good performance and 192 companies had inappropriate performance, and this difference is statistically significant. The value obtained for Z is also -5.33, and this value is not in H0 domain, so the H0 hypothesis is confirmed.

Financing is one of the issues raised by the launch of any new investment. Financing issues are especially important in developing countries. Developing countries need a lot of finance to advance in various economic areas. The results of this study indicate that outsource financing is related to company's performance. As it was stated, two variables of capital increase and bank loans are considered as outsource financing methods that are related to the performance of companies and in this study were considered as the main variables. In fact, companies are increasing their capital to be able to develop their activities and maintain and increase their competitive power. In some cases, this is also done to improve the company's financial structure. This new financing can be done in various forms. When a company in the stock exchange wants to increase its capital, it must publish a number of new shares and sell them to shareholders, in order to provide the amount needed for capital increase. Based on the results of the study, what increases the organization's performance in the organization is the optimal use of investment opportunities. The timely and reasonable use of investment opportunities has a significant effect on the performance of companies. The growth of the company in terms of the capital market and management, is an important variable and can affect its performance. Also, capital productivity deals with the measurement of the management ability in the optimal use of capital as one of the most important and limited resources of the company, and it is expected that the stocks of highly productive companies will also have a higher performance. Also, the results of the study showed that most of the companies that use bank loans as one of the financing methods, have had an inappropriate performance. In this method, usually all kinds risks threaten the company. In most cases, loans have a high interest rate, which also affects the companies' financial structure.

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IOSR Journal Of Humanities And Social Science (IOSR-JHSS) is UGC approved Journal with Sl. No. 5070, Journal no. 49323.

Mahdi Haghshenass Rezaie "A Study on the Relationship between Outsource Financing Processes and Companies' Performance." *IOSR Journal Of Humanities And Social Science (IOSR-JHSS)*. vol. 23 no. 04, 2018, pp. 41-47.