

CAPITAL STRUCTURE AND WORKING CAPITAL OF CASH HOLDING IN CONSUMER NON-CYCLICAL COMPANIES IN INDONESIA

Dinarossi Utami^{1*}, Belliwati kosim², Ervita Safitri³

^{1,2,3}Universitas Muhammadiyah Palembang

Jl. Jend. A. Yani 13 Ulu Palembang

***Email:** dinarossiutami@gmail.com

ABSTRACT

This research aims to expand previous literature regarding the impact of capital structure and working capital on cash holding. The research population comprised one hundred non-cyclical consumer companies from 2011 to 2022 and a sample of 55 companies with 266 observations. The research results show that working capital strongly influences the cash holding of non-cyclical consumer companies in Indonesia. This result is because it is related to the company's operational efficiency. Good operational management enables companies to maintain adequate liquidity, manage operational risks, and take advantage of existing opportunities without facing financial problems.

Keywords: Cash Holding, Capital Structure, Working Capital.

INTRODUCTION

Effective cash management is reflected in the management of cash holdings in the company. Cash holding is important for companies to ensure liquidity and flexibility, as well as the company's financial stability (Sun & Xia, 2022). In fact, companies can use cash as a hedging strategy to protect the company from market risks such as fluctuations in currency exchange rates or commodity prices. With adequate cash reserves, companies can deal with uncertainty, fund daily operations, take advantage of investment opportunities, and reduce dependence on external financing (Fawzi Shubita, 2019). Various reasons for research regarding cash holding are still carried out based on theoretical and practical scope. Theoretically, Trade-Off Theory is the basic theory for research on cash holding. Trade-off theory provides a comprehensive framework for understanding company decisions and determining the optimal amount of cash to hold (Alim, Kaleem, Abbas, & Khan, 2020). Trade-off theory states that a company will have cash up to the point where the marginal benefit of holding cash equals its marginal cost (Myers, 1977). This means companies need to balance the advantages and disadvantages of holding cash. By considering the benefits and costs of holding cash, this theory helps companies determine optimal cash levels to maximize liquidity and financial flexibility while minimizing opportunity costs and other risks. Practically, Trade-off theory provides practical guidance for financial managers to make balanced and informative decisions about cash management, which can be implemented in company financial policies. This theory can be adapted to various market conditions and business environments, so it remains relevant in multiple economic and

Proceeding 2nd Medan International Economics and Business

Volume 2, Issue 1, 2024

“Human Resource Transformation and Collaborative Innovation to Build Independent and Competitive Business in the Digital Era”

& Bakry, 2021). The independent variables of this research consist of capital structure and working capital, each of which has two measurement proxies. Then there are the control variables of this research, namely variables attached to the company, such as the number of company assets, number of employees, amount of capital, enterprise value, fixed assets, and market capitalization. The aim is to control or eliminate the influence of factors that could indirectly influence the results of the analysis or cause bias. The following is the research equation and Table 1 definitions of research variables.

$$CashNet_{it} = \alpha + \beta_1 Lev_{it} + \beta_2 LtDER_{it} + \beta_3 Ow_{it} + \beta_4 Nwc_{it} + \beta_5 C_{it} + \varepsilon_{it} \dots \dots (1)$$

$$CashTA_{it} = \alpha + \beta_1 Lev_{it} + \beta_2 LtDER_{it} + \beta_3 Ow_{it} + \beta_4 Nwc_{it} + \beta_5 C_{it} + \varepsilon_{it} \dots \dots (2)$$

Table 1. Variable Definition

Variable Name	Variable Abbreviation	Definition and Measurement
Cash Holdings	CashNet	The ratio of total cash and equivalents divided by (total assets–total cash and equivalents)
	CashTA	The ratio of cash and equivalents to total assets
Capital Structure	Lev	Total liabilities to total assets
	LtDER	Long-term debt to shareholder’s equity
Working Capital	Ow	The ratio of total operational current assets minus operational current liabilities
	Nwc	The ratio of current assets minus current liabilities divided by net total assets
Control Variabel	SzTA	Natural logarithm of total assets
	SzEmp	Natural logarithm of total employee
	FA	Natural logarithm of Total fixed asset
	EV	Natural logarithm of Enterprise value
	Cap	Natural logarithm of Capital
	MC	Natural logarithm of Market capitalization

Notes: ε_{it} is an error term

Based on the data structure used, namely panel data, testing is needed to choose the right analysis model. Panel or longitudinal data analysis is the subject of one of the most active and innovative bodies of econometric literature, in part because panel data provide a rich environment for the development of estimation techniques and theoretical results (Greene, 2014). Therefore, three estimation approaches can be taken: pooled OLS (common effect), fixed effect, and random effect estimates (Wooldridge, 2016).

Proceeding 2nd Medan International Economics and Business

Volume 2, Issue 1, 2024

“Human Resource Transformation and Collaborative Innovation to Build Independent and Competitive Business in the Digital Era”

RESULTS

The results of this research will provide an overview of the research data and estimation results of each research equation. The following is a statistical table for each variable used.

Tabel 2. Descriptive Statistics

Variable	Obs	Mean	Std. Dev.	Min	Max
CashNet	266	0.119	0.119	0.004	0.688
CashTA	266	0.098	0.084	0.004	0.404
Lev	266	0.396	0.119	0.093	0.81
LtDER	266	0.29	0.289	-0.25	1.556
Owc	266	3.059	0.083	2.711	3.214
Nwc	266	0.146	0.154	-0.46	0.537
SzTA	266	3.158	0.062	2.985	3.265
SzEmp	266	2.222	0.184	1.385	2.514
FA	266	3.126	0.074	2.882	3.24
Cap	266	3.042	0.053	2.772	3.141
EV	266	3.161	0.076	2.955	3.312
MC	266	3.146	0.084	2.929	3.312

Note: please see Table 1 for the description of variables.

Table 2 shows that almost all research variables have an average value greater than the standard deviation value. The CashNet and CashTA variables indicate that the majority of companies in the sample have good cash stability. This condition is an indicator of consistent cash management and shows good risk management. The capital structure and working capital variables also show low variability. This value indicates that most companies are close to the average value with few outliers. This condition also reflects that the company has a consistent funding policy and possibly has a well-managed funding strategy. In addition, the overall control variables of this study show that the companies have a similar operating scale, stable workforce size and funding structure, and the market assessment of the company is relatively stable and consistent.

Tabel 3. Result Estimation

Variables	CashNet	CashNet	CashTA	CashTA
Lev	-0.120*		-0.0712*	
	(0.0678)		(0.0430)	
LTDER	-0.00870		-0.00546	
	(0.00970)		(0.00616)	
Owc		-1.108***		-0.719***
		(0.178)		(0.112)
Nwc		0.435***		0.295***
		(0.0763)		(0.0477)
SzTA	7.374***	6.628***	4.761***	4.230***
	(0.913)	(0.902)	(0.579)	(0.564)

Proceeding 2nd Medan International Economics and Business

Volume 2, Issue 1, 2024

“Human Resource Transformation and Collaborative Innovation to Build Independent and Competitive Business in the Digital Era”

SzEmp	-0.628*** (0.185)	-0.637*** (0.164)	-0.384*** (0.117)	-0.393*** (0.103)
FA	-4.531*** (0.770)	-3.309*** (0.750)	-2.936*** (0.489)	-2.104*** (0.469)
EV	-4.715*** (0.771)	-2.985*** (0.695)	-3.380*** (0.489)	-2.192*** (0.435)
Cap	-1.380* (0.733)	-1.157* (0.635)	-0.839* (0.465)	-0.733* (0.397)
MC	2.531*** (0.632)	1.342** (0.545)	1.926*** (0.401)	1.103*** (0.341)
Constant	3.613* (2.044)	3.026* (1.745)	2.316* (1.298)	2.048* (1.092)
Observations	266	266	266	266
R-squared	0.364	0.499	0.394	0.536
Number of Company	55	55	55	55

Note: This table presents regression results using eq (1). Please see Table 1 for the description of variables. Superscripts ***, **, and * denotes statistically significant at the 0.01, 0.05 and 0.10 levels, respectively

After selecting the model by testing the Chow Test and Hausman Test, the fixed effect method is suitable for this research. In this research, the winzorization technique was also carried out to remove outlier data (Ochuko *et al.*, 2016), so that the total number of observations was 266 observations and a total of 55 companies. This research also carried out robustness testing so that the research estimation results can be declared robust. Table 3 shows the estimation results of the influence of capital structure and working capital, which have a significant effect on cash holding as a whole, based on the respective CashNet and CashTA equations. In the capital structure variable, the Lev proxy, which is the ratio of total liabilities to total assets, has a significant effect on CashNet and CashTA. However, the LtDER proxy, which shows a long-term debt to total shareholder's equity, does not affect CashNet and CashTA. In the working capital variable, the operating working capital and net working capital proxies each have a significant effect on CashNet and CashTA. Likewise, all control variables have a significant impact on the two proxies for cash holding.

Discussion

The Influence of Capital Structure on Cash Holding

Measuring capital structure with the Lev proxy has a significant influence on CashNet and CashTA. If Lev has a high value, then most of his assets are financed by debt. So, the company is usually at higher risk, which may affect the company's liquidity. High leverage can cause pressure on cash and cash equivalents because the company must meet debt obligations. This condition can reduce the ratio of cash and cash equivalents to total net assets, especially if the company does not have a strong operating cash flow to support debt payments. The results of this research indicate that a high ratio of total liabilities to total assets tends to have a negative influence on CashNet and CashTA. This negative impact is

Proceeding 2nd Medan International Economics and Business

Volume 2, Issue 1, 2024

“Human Resource Transformation and Collaborative Innovation to Build Independent and Competitive Business in the Digital Era”

caused by increased liquidity pressures and financial risks associated with high levels of debt. However, suppose the company has efficient management and a good financial management strategy. In that case, the company can minimize this negative impact and maintain a healthy level of cash and cash equivalents relative to total net assets. Measuring capital structure with the LtDER proxy, namely long-term debt to total shareholder's equity, does not affect CashNet and CashTA. LtDER is an indicator of a company's capital structure, which shows how much the company relies on long-term debt compared to equity to finance its assets. The lack of influence of LtDER on the two cash holding proxies is indicated by differences in focus between long-term funding and short-term liquidity management, as well as separate corporate financial management strategies. Such as long-term debt, which may be used for capital investment or long-term projects, while cash and cash equivalents are managed for daily operational needs.

The Influence of Working Capital on Cash Holding

This research's working capital measurement uses operating working capital and net working capital proxies. The two working capital proxies each have a significant effect on the two cash holding proxies, namely CashNet and CashTA. This condition shows that the company has good working capital management. A high level of operating working capital indicates that the company invests a lot of assets in daily operations, such as inventory and accounts receivable. This condition can reduce the amount of cash available because more current assets are tied up in operations. Apart from that, if the company can manage operating working capital efficiently, the company can free up more cash. For example, speeding up the collection of accounts receivable or reducing inventory can increase available cash. Furthermore, if the company has high net working capital, it is indicated that the company has more current assets than current liabilities. So, companies tend to have more cash reserves to meet short-term obligations. In addition, if a company uses most of its current assets for operations, then the company can reduce the amount of cash available. Effective working capital management can ensure that a company does not tie up too much cash in non-cash current assets. A company with high net working capital has more current assets compared to current liabilities, giving it more flexibility to hold cash. This condition means the company may have larger cash reserves to address sudden needs or investment opportunities. Overall, the control variables in this study have a significant effect on both proxies for cash holding. The use of this control variable aims to ensure that the analysis results reflect a real relationship between the independent and dependent variables and are not due to undesirable external factors.

CONCLUSION

Based on the results and discussions that have been carried out, it can be concluded that there is a significant influence on capital structure and working capital on cash holding. Capital structure influences cash storage decisions, so if the company can manage it well, then it can ensure its long-term financial health. Apart from that, effective working capital management is also very important to ensure the company has sufficient liquidity for operations and financial flexibility, which ultimately affects the company's cash holding level. This research has limitations in the period and scope of the study, as it is only in the

Proceeding 2nd Medan International Economics and Business

Volume 2, Issue 1, 2024

“Human Resource Transformation and Collaborative Innovation to Build Independent and Competitive Business in the Digital Era”

Consumer Non-Cyclical sector. So, it is hoped that there will be additional scope for further research.

REFERENCES

- Akhtar, T., Chen, L., & Tareq, M. A. (2024). Blockchain technology enterprises' ownership structure and cash holdings. *Sustainable Futures*, 8. <https://doi.org/10.1016/j.sftr.2024.100229>
- Alim, W., Kaleem, M., Abbas, S., & Khan, D. (2020). Do capital structure and cash holding expropriate minority shareholders? A case of non-financial concentrated firms in Pakistan. *Journal of Financial Crime*, 27(4), 1289–1305. <https://doi.org/10.1108/JFC-03-2020-0033>
- Alnori, F., Bugshan, A., & Bakry, W. (2022). The determinants of corporate cash holdings: evidence from Shariah-compliant and non-Shariah-compliant corporations. *Managerial Finance*, 48(3), 429–450. <https://doi.org/10.1108/MF-02-2021-0085>
- Anh, P. T. L., Hung, D. N., & Binh, V. T. T. (2023). Relationship between cash holding and capital structure of Vietnamese public companies in the COVID-19 pandemic context. *Investment Management and Financial Innovations*, 20(3), 212–223. [https://doi.org/10.21511/imfi.20\(3\).2023.18](https://doi.org/10.21511/imfi.20(3).2023.18)
- Basheer, M. F., Waemustafa, W., & Ahmad, A. A. (2018). The paradox of managerial ownership and financial decisions of the textile sector: An Asian market perspective. *Journal of Social Sciences Research*, 2018(Special Issue 4), 184–190. <https://doi.org/10.32861/jssr.spi4.184.190>
- Bugshan, A., Alnori, F., & Bakry, W. (2021). Shariah compliance and corporate cash holdings. *Research in International Business and Finance*, 56. <https://doi.org/10.1016/j.ribaf.2021.101383>
- Diaw, A. (2021). Corporate cash holdings in emerging markets. *Borsa Istanbul Review*, 21(2), 139–148. <https://doi.org/10.1016/j.bir.2020.09.005>
- Farooq, U., Yang, Y., & Xie, H. (2023). Asymmetric effect of renewable and non-renewable energy consumptions on corporate cash holdings: new panel data evidence from BRICS economies. *Kybernetes*. <https://doi.org/10.1108/K-02-2023-0216>
- Fawzi Shubita, M. (2019). The impact of working capital management on cash holdings of large and small firms: Evidence from Jordan. *Investment Management and Financial Innovations*, 16(3), 76–86. [https://doi.org/10.21511/imfi.16\(3\).2019.08](https://doi.org/10.21511/imfi.16(3).2019.08)
- Greene, W. H. (2014). *Econometric Analysis*. In Prentice Hall.
- Lu, C.-L., Chen, H.-C., Chou, R. K., & Lin, C.-Y. (2023). Debt capacity, cash holdings and financial constraints. *Journal of Business Finance and Accounting*. <https://doi.org/10.1111/jbfa.12771>
- Mouline, B., & Sadok, H. (2021). Determinants of corporate cash holdings: Evidence from the Moroccan market. *Accounting*, 7(6), 1231–1240. <https://doi.org/10.5267/j.ac.2021.4.017>
- Myers, S. C. (1977). Determinants of corporate borrowing. *Journal of Financial Economics*, 5(2), 147–175. [https://doi.org/10.1016/0304-405X\(77\)90015-0](https://doi.org/10.1016/0304-405X(77)90015-0)
- Rama Iyer, S., Sankaran, H., & Walsh, S. T. (2020). Influence of Director Expertise on Capital Structure and Cash Holdings in High-Tech Firms. *Technological Forecasting and Social Change*, 158. <https://doi.org/10.1016/j.techfore.2020.120060>
- Rösl, G., & Seitz, F. (2024). Uncertainty, politics, and crises: The case for cash. *Latin American Journal of Central Banking*, 5(3). <https://doi.org/10.1016/j.latcb.2024.100128>
- Shubita, M. F. (2019). *The impact of working capital management on cash holdings of large and small firms : evidence from Jordan*. [https://doi.org/10.21511/imfi.16\(3\).2019.08](https://doi.org/10.21511/imfi.16(3).2019.08)
- Singh, N. (2018). Effect of Cash Holding Policy of Financially Constrained Firms on Their Market Performance. *Management and Labour Studies*, 43(1–2), 31–45. <https://doi.org/10.1177/0258042X17747783>

Proceeding 2nd Medan International Economics and Business

Volume 2, Issue 1, 2024

“Human Resource Transformation and Collaborative Innovation to Build Independent and Competitive Business in the Digital Era”

- Sun, Q., & Xia, J. (2022). Cash Holdings, Capital Structure, and Financing Risk. *Journal of Financial and Quantitative Analysis*, 57(2), 790–824. <https://doi.org/10.1017/S002210902000099X>
- Wooldridge, J. M. (2016). Introductory Econometrics, A Modern Approach. In *South-Western Cengage Learning* (Sixth Edit).
- Yin, J., & Yang, X. (2023). How Does Corporate Social Responsibility Affect Corporate Cash Holdings? *Emerging Markets Finance and Trade*, 59(10), 3201–3219. <https://doi.org/10.1080/1540496X.2023.2212841>
- Zhang, R. (2020). Trade credit, cash holdings, and product market competition. *Quarterly Review of Economics and Finance*, 78(April 2007), 132–146. <https://doi.org/10.1016/j.qref.2020.01.006>