Is Capital Structure Important in Contemporary Finance Relations?

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Abstract The various combinations of sources of financing that a business uses in its operations have multiple impacts on the generation of its cash flow. Such influence can be viewed from the aspect of forming the total cost of financing the company, from the aspect of investments where such an indicators represents the minimum level of required profitability of investment projects, as well as from the aspect of investors in an enterprise where different capital structure carries with it a different level of financial risk. It is therefore not surprising that there is considerable scientific interest in this issue and numerous researches conducted on this topic. Moreover, the relevance of the subject is also evidenced by the fact that there are numerous theories on the formation of capital structure and its consequences on the valuation of the company, that is, the influence on the market value of the company's shares.

This paper will determine the average values of the formation of the capital and financial structure of Croatian companies listed on the Zagreb Stock Exchange. The analysis of 30 companies over a ten-year period from 2009 to 2018 will seek to show the impact that the formed capital structure has on profitability. By establishing a negative link between the selected debt indicators and the profitability indicators, the validity of contemporary capital structure theories, which have their starting point in behavioral finance and are specific for developed financial markets, has been rejected.

Keywords:
capital structure, financial structure, debt ratios, profitability ratios, capital structure theories.

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1 Introduction

In addition to defining investment and profit-sharing (dividend) policies, financing policy is the third strategic issue facing the management of each company. The financing policy determines the available and desired sources of financing available to the enterprise, as well as the desired combination of these same sources. Namely, numerous existing theories regarding the formation of the optimal structure of financial sources are indicative proof of the actuality of the question posed, as well as of the potential solutions to the dilemma.

However, the main distribution of financing sources is to other sources of financing (debt) and to own sources of financing (equity), as well as the repercussions that different combinations of the two groups have on the overall performance of the company. In the context of this research, emphasis will be placed on determining their impact on the profitability of business. In accordance with the obtained results, an attempt will be made to answer the eternal question of the justification of certain theories of capital structure and their provability on concrete data.

In addition to the issues related to the formation of the financial structure of companies and their interpretation within the existing theories of capital structure, this paper will also give a brief overview of the conclusions reached in the context of contemporary finance. Why is this important to determine? The answer lies in the fact that there are significant differences between the developed financial markets of the Western world and the rudimentary emerging financial markets, which Croatian market obviously belongs to. The aspiration of the Republic of Croatia to modern political trends should not stop with declarative membership to the European Union, the common market, as well as a probable monetary union, but should also spill over into economic flows, which should thus become as similar to those of the developed western countries. In that case, the results obtained by analyzing the Croatian capital market should be similar to those obtained by analyzing contemporary financial and capital markets.

Is that so, it can be seen by following this brief analysis organized as follows. A chapter in which the capital and financial structure of an enterprise will be terminologically defined, with its different coverage and universal interpretation, follows this introductory section. The following is a chapter with methodological

notes related to the conduct of the research, followed by a chapter in which the structure and composition of the financial and capital structure of the sample companies are analyzed with empirical data. The analysis is continued by determining the correlation coefficients between the selected indicators of the financial structure and the realized profitability of the analyzed companies in order to arrive at an answer on the acceptability or unacceptability of certain theories of capital structure. The paper conclude with a concluding discussion and an overview of the bibliographic units used.

2 Different understanding of the capital and financial structure of the company

Often, in papers describing the various sources of financing that are available to a company, the terms financial and capital structure are used synonymously. These terms mean the ratio of its own and other sources of financing used by the company and recorded in the liabilities of its balance sheet. Sometimes such a conceptualization is justified, especially if the basic principles derived from capital structure theories are applied to the entire sources of corporate financing, and sometimes this is totally unjustified by exempting the entire short-term segment of debt financing.

From the previous statement, it is possible to notice the conceptual distinction between the two. Specifically, capital structure means the ratio of debt to equity used by an entity to finance its long-term operations. In other words, the capital structure implies the relation between own permanent sources of financing (for example ordinary shares, retained earnings, reserves) and long-term debt financial arrangements of an enterprise (for example bonds, loans, etc.).[1]

On the other hand, the financial structure is a broader term because, in addition to the long-term elements covered by the capital structure, it also covers short-term sources of financing. The financial structure is therefore referred to as different combinations of total debt and own sources of financing recorded on the liability side of the company's balance sheet. Debt category means the total amount of other

[1] See, for example, OOi, J. (1999): The Determinants of Capital Structure: Evidence on UK Property Companies, *Journal of Property Investment and Finance*, 17, 5, 464-480. or Harris, M., Raviv, A. (1991): The Theory of Capital Structure, *Journal of Finance*, 46, 1, 297-355.

sources of financing (debt) irrespective of their maturity, while the coverage of equity is identical to that on the capital structure.[2]

Hereafter, the terms capital structure and financial structures will be used synonymously. The coverage of the analyzed data corresponds to the one defined by financial structure, and in explaining their impact the conclusions of capital structure theories are used. Such a duality of data coverage and interpretation is justified in this case, since the results of the analysis of this paper remain in the sphere of aggregate level.

The financial (and capital) structure has long been the subject of interest of many scholars and practitioners, given its importance in determining the value of company. The reason for this lies in the multiple implications that different combinations of possible sources of financing have on its operating costs, its realized financial result, and on the degree of perceived riskiness, that consequently affects the market value of the company's shares. The consequences of increasing the level of indebtedness include an increase in financial risk, a decrease in credit rating and an increase in financing costs. This should ultimately result in a reduced profit for the company and consequently a drop in the market price of the shares.

A decrease in the level of indebtedness, i.e. an increase in the level of own financing, will result in an increase in the company's liquidity, the formation of certain solvency reserves, all of which will contribute to a decrease in the expected rate of return used in discounting the company's future cash flows. Furthermore, there is a rational expectation that all of this will contribute to an increase in the future level of profit that investors in the market will reward with an increase in the market price of the shares.

However, the different structure of the financial (and capital) structure of the company is also a consequence of various other business decisions. The reasons for this lie in the day-to-day decisions of the management on the sources of settlement of its financial obligations, as well as on the decisions on financing investment

[2] For definition, see Flannery, M.J., Rangan, K.P. (2006): Partial Adjustment toward Target Capital Structures, *Journal of Financial Economics*, 79, 3, 469-506. or Bevan, A.A., Danbolt, J. (2000): Capital Structure and its Determinants in the United Kingdom – A Decompositional Analysis, *University of Glasgow Working Paper*, No. 2000-2, May 2000., http://ssrn.com/abstract=233550 (30.11.2019.)

projects. Therefore, the aforementioned causal relationship does not have to be unambiguous and exclusive.

3 Research methodology

Given the stated objective of this research to determine the impact of the capital and financial structure on the profitability of Croatian companies, it was necessary to determine a representative sample of shares from the Zagreb Stock Exchange. For this purpose, the basic share's liquidity criterion was set, i.e. that the share was traded at least once a week. Such a criterion of liquidity was satisfied mainly by the shares included in the CROBEX share index with the addition of several shares not included in the share market index. Excluded from the consideration are shares of the financial sector (banks and insurance companies) whose financial structure is formed in accordance with some other principles and therefore does not correspond to the implementation in the desired research. The final list of shares forming the sample can be seen in Table 1.

Table 1: List of companies in a sample.

Ticker	*Company*	*Ticker*	*Company*
ADPL	AD Plastik d.d.	**LRH**	Liburnia Riviera hoteli d.d.
ADRS	Adris grupa d.d.	**LRHC**	FTB turizam d.d.
ARNT	Arenaturist d.d.	**MAIS**	Maistra d.d.
ATGR	Atlantic grupa d.d.	**MDKA**	Medika d.d.
ATLN	Excelsa nekretnine d.d.	**OPTE**	OT – Optima telekom d.d.
ATPL	Atlantska plovidba d.d.	**PLAG**	Plava laguna d.d.
DDJH	Đuro Đaković holding d.d.	**PODR**	Podravka d.d.
DLKV	Dalekovod d.d.	**PTKM**	Petrokemija d.d.
ERNT	Ericsson Nikola Tesla d.d.	**RIVP**	Valamar riviera d.d.
HT	Hrvatski Telekom d.d.	**THNK**	Tehnika d.d.
IGH	Institut IGH d.d.	**TPNG**	Tankerska next generation d.d.
INA	INA – Industrija nafte d.d.	**ULPL**	Uljanik Plovidba d.d.
INGR	Ingra d.d.	**VART**	Varteks d.d.
KOEI	Končar-elektroindustrija d.d.	**VIRO**	Viro tvornica šećera d.d.
KRAS	Kraš d.d.	**VLEN**	Brodogradilište Viktor Lenac d.d.

Source: Zagreb Stock Exchange at www.zse.hr

The analysis of the sample companies was carried out for the period 2009 to 2018, except for the TPNG and LRHC shares, which were listed on the Zagreb Stock Exchange later, respectively in 2014 and 2015. The analysis was performed by calculating the financial ratios shown in Table 2 using the audited and consolidated financial statements that the companies themselves submit to the Zagreb Stock Exchange. The first three indicators in Table 2 have been calculated to represent the financial (capital) structure of an company, while the last two indicators are indicators of the company's profitability.

Table 2: Display of the financial indicators calculation.

Indicator	*Numerator*	*Denominator*
Debt ratio (LEV)	total liabilities – capital and reserves	total assets
Financing ratio (FIN)	total liabilities – capital and reserves	equity
Long-term balance (LTB)	long-term assets	long-term liabilities + capital and reserves
Return on assets (ROA)	net profit – prefered dividends	total assets
Return on equity (ROE)	net profit – prefered dividends	equity

Source: Žager, K., Mamić Sačer, I., Sever, S., Žager, L. (2009): *Analiza financijskih izvještaja*, Masmedia, Zagreb, p. 251.

4 Analysis of the capital and financial structure for the companies in sample

Before determining the causal relationship between a company's capital structure and its profitability, it is necessary to consider the structure of the company's financing sources, as well as the horizontal cross-section of the company's balance sheet in terms of establishing short- and long-term balance sheet equilibrium. The results shown in Table 3 represent the average values calculated for all companies in the sample for the analyzed period.

The columns in the table displaying the financial structure show the percentages of each available source of financing related to total liabilities. These sources of financing are presented through the following groups: capital and reserves (CAP),

long-term liabilities (LTL) and short-term liabilities (STL). The last two columns in the table show the long-term (LTB) and short-term (STB) balance sheet equilibrium calculated in the manner shown in Table 2, respectively:

$$STB = \frac{Short\ term\ assets}{Short\ term\ liabilities}$$

Table 3: Financial structure of the sample companies.

Ticker	Financial structure (in %)			Balance sheet equilibrium	
	CAP	*LTL*	*STL*	*LTB*	*STB*
ADPL	53,35	14,77	31,88	0,99	1,11
ADRS	69,93	14,63	15,44	0,72	3,13
ARNT	64,32	28,39	7,29	1,00	1,75
ATGR	37,33	35,76	26,91	0,80	1,70
ATLN	88,86	7,99	3,2	0,87	11,51
ATPL	44,22	41,38	14,40	1,08	0,78
DDJH	20,75	32,67	46,58	0,94	1,34
DLKV	16,64	25,11	58,25	2,53	0,98
ERNT	66,40	2,11	31,49	0,43	3,81
HT	84,79	2,05	13,16	0,72	3,11
IGH	9,54	43,86	46,60	1,06	1,06
INA	59,54	9,36	31,10	1,30	0,93
INGR	14,81	42,07	43,11	1,45	0,56
KOEI	73,34	4,16	22,50	0,64	6,49
KRAS	55,17	14,04	30,78	0,81	1,47
LRH	84,75	9,62	5,62	0,99	1,49
LRHC	57,11	32,71	10,17	1,01	1,42
MAIS	52,29	4,23	43,50	1,82	0,06
MDKA	20,81	4,54	74,65	0,81	1,07
OPTE	6,87	60,82	32,30	1,27	0,90
PLAG	79,13	14,38	6,48	0,97	1,73
PODR	51,71	19,35	28,93	0,74	1,89
PTKM	22,64	13,06	64,30	1,96	0,86
RIVP	58,12	33,35	8,53	1,03	1,00
THNK	23,73	23,96	52,31	1,13	1,13
TPNG	47,88	46,18	5,94	1,00	1,07
ULPL	17,69	67,32	14,99	1,20	0,28
VART	37,82	24,96	37,22	1,35	0,57
VIRO	34,91	17,55	47,54	0,89	1,40
VLEN	60,59	14,41	25,00	0,87	1,52
Average	**47,17**	**23,49**	**29,34**	/	/

Source: Author's calculation

An analysis of the data in Table 3 reveals a good commitment on the part of the management of the company to combine the sources of financing in the way of managing the financial and capital structure of the enterprise. More than half of the sample companies use their own sources of financing (equity plus reserves) as the dominant source of funds for doing business. The high percentage of own funds in the financial structure is also evident from its average value, which for the analyzed companies amounts to 47,17%. After them, short-term liabilities represent the second most significant source of financing with an average value of 29,34%, while long-term liabilities represent on average 23,49% of the engaged sources of financing in the analyzed companies.

This arrangement of engaged sources of financing is a good indicator that companies are thinking about the financial risk they are exposed to and have roughly the same percentage of their own and other sources of financing. In this way, companies are insured in case of unforeseen circumstances, where a high percentage of their own funds should serve as a kind of "capital cushion", similar to the principle of bank operations. It is also interesting to note that, for the most part, the largest number of companies with percentages of own funding (CAP) higher than average, and generally greater that 50%, belong to the industry and tourism sectors.

An additional argument of generally sound management of the financial structure, but also of the related items in the balance sheet assets, can be obtained through the analysis of the balance sheet equilibrium. The "golden balance sheet rule" states that in perfect market conditions, the value of current assets should be equal to the value of current liabilities as this would achieve a short-term equilibrium. The same principle applies to the ratio of long-term assets to long-term liabilities. With such a horizontal cross-section of the corporate balance sheet, the overall cost of financing should be minimum and, accordingly, the value of company should be maximized. Fulfillment of this rule would mean that the LTB and STB indicators are equal to 1.

The obtained results show that the value of these indicators deviates from the theoretical level and differs from the value of 1. Such a deviation is desirable for companies that operate in real, rather than perfect conditions, in such a way that certain solvency reserves are formed and the occasional bridging is enabled for periods of mismatch between cash receipts and cash outflows. In order to solvency

reserves been formed, a deviation from the "golden balance sheet rule" is required as follows: LTB < 1 and STB > 1.

This deviation of the STB indicator indicates a situation in which a company's current assets are greater that its current liabilities, thus providing slightly higher cash receipts that cash expenditures over the same period of time. On the other hand, the deviation of the LTB indicator indicates a situation in which a company's long-term available finance (long-term liabilities plus equity and reserves) are greater than the value of its fixed assets. Following the logic of the timing of cash receipts and cash outflows, this situation implies that some of the current assets were acquired from long-term sources of financing. This refers to permanent current assets that will generate cash receipts over a period of more than 1 year, even though according to their purchasing value are classified as current assets.

The results of these indicators in Table 3 confirm that the sample companies on average largely account for the timing of cash receipts and cash expenditures, hence the financial risk translated into liquidity risk. This is evident because 15 companies in full, and additional two companies' borderline, meet the criterion of long-term balance sheet imbalance (LTB < 1). Under the short-term balance sheet imbalance criterion (STB > 1), the result is even more evident as 21 out of 30 sample companies meet the required inequality.

5 Relationship between financial structure and profitability of Croatian companies

Further analysis focuses on the calculation of the indicators defined in Table 2, as well as the correlation between the calculated indicators. The calculation of correlation coefficients seeks to determine whether there is a correlation between the selected indicators of financial structure and the achieved profitability of the sample companies. The calculated indicators are shown in Table 4 and represent the average values for the analyzed ten-year period.

With regard to financial structure indicators, particular attention will be paid to the analysis of the LEV and FIN indicators, since the movement of the LTB indicator has already been analyzed when interpreting the data in Table 3. Namely, this indicator is shown in this table again because it will be included in a later analysis

regarding correlation between financial structure indicators and reported profitability of companies. From the previous analysis, it is sufficient to mention that the long-term balance sheet equilibrium indicator (LTB) indicated management's concern about financial risk in a way that they kept track of the timing of cash receipts and cash expenditures.

Table 4: Average values of selected indicators for the sample companies, years 2009-2018.

Ticker	Financial structure			Profitability	
	LEV	*FIN*	*LTB*	*ROA*	*ROE*
ADPL	0.476	1.528	0.99	0.0361	0.1131
ADRS	0.323	33.202	0.723	0.0433	3.2915
ARNT	0.377	10.49	1.001	-0.0038	-0.1527
ATGR	0.641	23.858	0.801	0.0357	1.273
ATLN	0.129	0.276	0.869	0.0782	0.1642
ATPL	0.563	3.059	1.084	-0.0517	-0.2817
DDJH	0.799	2.323	0.937	-0.0796	-0.2299
DLKV	0.837	5.982	2.533	-0.0483	-0.3046
ERNT	0.457	3.201	0.426	0.0975	0.6929
HT	0.176	0.279	0.718	0.0984	0.1583
IGH	0.904	9.199	1.063	-0.0797	-0.6275
INA	0.497	1.402	1.301	0.0012	0.008
INGR	0.856	5.301	1.453	-0.02	-0.0805
KOEI	0.367	1.15	0.64	0.0445	0.1361
KRAS	0.454	0.98	0.812	0.0195	0.0416
LRH	0.169	0.213	0.999	0.0046	0.0071
LRHC	0.448	0.973	1.014	0.018	0.041
MAIS	0.497	0.992	1.823	0.0308	0.0706
MDKA	0.792	15.601	0.815	0.02	0.357
OPTE	1.389	19.733	0.004	-0.0564	-1.3421
PLAG	0.216	0.437	0.972	0.0576	0.1055
PODR	0.502	1.425	0.743	0.0147	0.0511
PTKM	0.778	5.316	1.962	-0.1516	-1.144
RIVP	0.434	1.09	1.034	0.0202	0.0574
THNK	0.784	5.4	1.132	-0.065	-0.2744
TPNG	0.523	1.615	1.001	0.0208	0.0639
ULPL	0.831	5.42	1.201	-0.0723	-0.3893
VART	0.625	4.338	1.354	-0.0665	-0.4506
VIRO	0.662	3.775	0.893	-0.0175	-0.0584
VLEN	0.41	0.922	0.874	0.0077	0.02

Source: Author's calculation

Regarding the LEV and FIN indicators, both indicate the debt structure and show the ratio of utilization of other sources of financing put in relation to the total assets,

i.e. the equity of the company. Conservatively, it is considered that the LEV indicator should be less than or equal to 50% (or 0,5), and that the FIN indicator should be less than or equal to 1. Such indicator values would indicate a financial structure that would even in the most unfavorable situation of bankruptcy and liquidation, enable all creditors to settle down their claims from company's own equity.

A more modern understanding of corporate finance also accepts a deviation from this rigorous criterion in a way that it consider acceptable if the value of LEV < 70%, or the value of FIN < 2,3. Such ratios indicate a financial structure where as much as 70% of all financing comes from other sources (debt), while the acceptable level of capital is at least 30%. This is especially pronounced for those companies that have a lot of real estate in their property, so it is logical that they have higher levels of debt. However, as this debt is secured mostly by a mortgage, the total perceived financial risk exposure is not as pronounced.

The level of these indicators for the sample companies indicate a prevailing contemporary understanding of the debt problem. Specifically, according to conservative criteria, half of the sample (15 companies) holds its LEV indicator below 50%, while for FIN indicator, only 8 companies meet the criterion that the value is less than 1. Modern criteria for acceptable level of these indicators have been met by 21 companies for the LEV indicator, i.e. 15 companies for the FIN indicator.

In terms of profitability indicators, their interpretation is fairly clear. The higher their value, the better the position of the company in terms of the realized profit put in relation to the total assets, i.e. own capital. As the past 10-year period has been marked by significant financial turmoil, unfortunately, many companies report average losses, and few are companies that have achieved double-digit returns in the analyzed period.

A further step in proving the stated objective of the research is to identify the link between the way in which the financial structure is formed and the business result achieved by these companies through such a financial structure. This was done by calculating the correlation coefficients between the selected indicators and shown in Table 5.

Table 5: Correlation coefficients of selected indicators of financial structure and profitability.

LEV	*FIN*	*LTB*	*ROA*	*ROE*	
1.0000	0.3452*	0.0910	-0.6977***	-0.4685***	*LEV*
	1.0000	-0.2341	-0.0705	0.5236***	*FIN*
		1.0000	-0.4331**	-0.2257	*LTB*
			1.0000	0.5748***	*ROA*
				1.0000	*ROE*

Note: *** significant at the 0.01 level; ** significant at the 0.05 level; * significant at the 0.10 level
Source: Author's calculation

It is interesting to monitor the movements of the correlation coefficients between indicators belonging to two separate groups. Such indicators are generally negative and significant, which in the case of LEV indicator indicates that any further increase in the level of indebtedness will have a negative effect on the profitability indicators of ROA and ROE. A further increase in LTB indicator will have the same negative impact.

The situation with the FIN indicator is somewhat different because it produces contradictory results: a negative correlation coefficient with the ROA indicator and a positive one with the ROE indicator. Preference should however be given to a positive indicator that is highly significant. An interpretation of this value should be sought in the aforementioned contemporary understanding of the permissible indebtedness limits used by the sample companies to finance real estate purchase. Acquisition of real estate by debt financing which to the same extent increases company's total liabilities and its total assets, will not affect the change in the debt ratio. Moreover, it is understood that such real estate will have a profitability higher than the average weighted cost of capital, thus justifying the investment in them. This will lead to an increase in the numerator of FIN indicator, preserving the same value of denominator, resulting in an increase in the FIN ratio, which contributes to an increase in profitability (ROE indicator).

The results obtained throughout the analysis conducted in this paper could be put in the context of proving or refuting existing capital structure theories. Namely, the results cannot be used to reach a conclusion as to which theory of capital structure has been proven, but what can be deduced is which of the existing theories has not been proven through the data analyzed. These are the theories that basically argue

that there is no correlation between the sources of financing and how to combine the financial structure, with the value of the company itself.

As the obtained results indicate that the correlation between the capital structure and the financial result exists, as well as the value of the company, it can be concluded that no evidence was found on the Croatian capital market to substantiate the Modigliani-Miller theory of the irrelevance of the capital structure (tax-free version)[3], Signal theory[4], as well as Pecking order theory[5].

Furthermore, the analysis did not find any evidence to support the validity of the Modigliani-Miller theory of the irrelevance of the capital structure with taxes involved. Namely, according to this theory, the optimal capital structure would be one that would be fully financed by debt because in that case the tax shelter would be maximal. However, since the sample companies keep their indebtedness at acceptable level, and any further increase in their indebtedness results in a decrease in profitability indicators (seen in Table 5), there is no evidence to support this theory.

What the analysis so far suggests, however, is that all the research findings can best be explained by behavior in accordance with Trade-off theory of capital structure. This theory assumes that there is some level of indebtedness that is optimal because at this level a minimum weighted average cost of capital is achieved, and the value of the company is maximized. Elements that influence the finding of the optimal level of indebtedness are the tax shelter on one hand, and the cost of financial distress and the agency costs on the other.[6]

Any further increase in the level of indebtedness beyond the optima limit would have a negative effect on the value of the company, i.e. its profitability (visible from

[3] Modigliani, F., Miller, M.H. (1958): The Cost of Capital, Corporation Finance and the Theory of Investment, *American Economic Review*, 48, 3, 261-297.
[4] Ross, S.A. (1977): The Determination of Financial Structure: The Incentive Signaling Approach, *Bell Journal of Economics*, 8, 1, 23-40.
[5] Myers, S.C. (1984): The Capital Structure Puzzle, *Journal of Finance*, 39, 3, 575-592. and Myers, S.C., Majluf, N. (1984): Corporate Financing and Investment Decisions When Firms Have Information That Investors Do Not Have, *Journal of Financial Economics*, 13, 2, 187-221.
[6] See, for example, Baxter, N.D. (1967): Leverage, Risk of Ruin and the Cost of Capital, *Journal of Finance*, 22, 3, 395-403.; Scott, J.H. (1976): A Theory of Optimal Capital Structure, *Bell Journal of Economic and Management Science*, 7, 1, 33-54.; Brennan, M.J., Schwartz, E.S. (1978): Corporate Income Taxes, Valuation, and the Problem of Optimal Capital Structure, *Journal of Business*, 51, 1, 103-114.

the negative correlation coefficients of LEV and LTB indicators). The optimal level of indebtedness is at some level higher than 50% as suggested by the traditional approach to capital structure, but still below 100% as suggested by Modigliani-Miller's irrelevance theory of capital structure with taxes included. The results show that the average level of indebtedness (LEV indicator) for all companies in the sample is almost 53%.

The only way to significantly increase the value of a company according to this, and other theories as well, is to adopt profitable investment projects that achieve their profitability at levels higher than the weighted average cost of capital. This is evident from the sign of the correlation coefficient regarding FIN indicator, the explanation and interpretation of which has already been given in the previous paragraphs.

6 Conclusion

Instead of the classic conclusion, here it is necessary to return to the very title of this article and ask ourselves what evidence we have come to in trying to answer the question about the importance of capital structure in contemporary finance. The results obtained indicated a significant negative relationship between the degree of indebtedness and the profitability indicators. Furthermore, the negative correlation coefficient between the long-term balance sheet equilibrium and profitability indicators indicates the need for careful deliberation when choosing a source of financing.

The positive coefficient of correlation between the financing ratio and profitability indicator ROE emphasizes the possibility of financing the procurement of assets from other sources of financing, even in the percentage that exceeds traditional framework. Of course, the profitability of such projects is important, which with the increasing share of debt in the financing structure, is becoming more and more available, due to the increasing usage of tax shelter which has the effect of reducing the average weighted cost of capital.

Combining all the fact obtained, it follows that it is the best to use the determinants of the Trade-off theory of capital structure to explain the results obtained. Therefore, we return to the beginning and answer the question from the title of this paper. Trade-off theory, according to its settings, still falls into the category of so-

called traditional financial theories that seek to rationally and objectively quantify scientific knowledge.

No evidence has been found for the theories of contemporary finance, which have elements of behavioral finance in their settings. Whether the reason is a specific period of analysis that captures the impact of the global financial and economic crisis, or the reason lie in the emerging financial market characteristics, which Croatian capital market is, remains an unanswered question. In any case, the analysis proved that the Croatian capital market is still rudimentary, low capitalized, with a small number of liquid shares, and as such, it is still separated from contemporary developments characteristic for developed capital markets.

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