

**Topic: Capital Structure, Investment Decisions,
and Business Value.**

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1. Introduction

Financial management plays an essential role in helping organisations perform efficiently, maintain stability, remain competitive, and increase their value. Financial management entails strategic decision-making when planning, acquiring, distributing, and controlling finances (Bisht et al., 2022). Organisations have to determine where to invest, how to fund their operations, whether they should opt for debt or equity financing, and the risks they are willing to take. Such decisions impact the cost of capital, profitability, cash flows, returns on investments, and the organisation's overall value. The capital structure includes the proportion of debt and equity used by an organisation to acquire funds. The cost of debt is lower than that of equity, making the former more attractive. Nevertheless, debt creates more repayment obligations, while equity decreases them. As a result, managers need to consider both sources appropriately. Organisations can also make investment decisions when acquiring new technologies, expanding their businesses, making mergers, investing in new projects, or enhancing production efficiency (Suo et al., 2023). Due to uncertainties involved, managers apply various methods like net present value, internal rate of return, payback period, and profitability index. In this report, it is argued that the relationship between capital structure and investment decisions is quite strong since the former affects the latter in terms of cost of capital, risk, investment opportunities, and business value. The purpose of this report is to explore the impact of capital structure and investment decisions on business value. The topics discussed include debt, equity, risk, returns, investment evaluation, cost of capital, shareholder value, and sustainability.

2. Literature Review

The theoretical background is presented by means of a review of the relevant literature in order to provide insights into the impact that capital structure, investments, cost of capital, and risk have on the overall value of businesses. Theory is vital to financial management because it can help understand why organizations adopt specific sources of financing, what their decision-making processes with respect to investments are, and how these factors impact shareholder value and sustainability. The current chapter hence moves beyond the basic definitions and critically evaluates some of the central concepts of financial management such as the goals of financial management, theories of capital structure, financing with debt and equity, investment appraisal methods, weighted average cost of capital, and shareholder value and sustainability.

2.1 Objectives of Financial Management

Traditionally, the aim of financial management was the maximization of shareholder wealth. It implies that a company's decision-makers have to make decisions which will bring profits to shareholders. In other words, every single financial decision has to be evaluated according to how it can make an organization earn more, increase its market value, and yield returns that exceed the cost of capital. For instance, the project is supposed to bring additional profits only if it is expected to generate some positive economic outcome despite costs, risks, and opportunities. However, in reality, financial management does not only involve shareholder returns. Any company works in an environment when its performance depends not only on its financial status and profit but also on its customers, employees, creditors, regulators, suppliers, and even community (Mahandani & Su, 2025). That is why it is crucial for a financial manager to consider all the possible factors related to stakeholders and sustainable development. Even though any project might bring short-run profits, it might negatively impact its sustainable value. The duties of a financial manager include making investment decisions, financing decisions, dividend decisions, managing risks, managing working capital, and evaluating performance. In terms of investment decision making, the task involves the selection of projects that will yield future gains, whereas, in financing decisions, one has to choose among debt, equity, or retained earnings. In the case of dividend decision making, one has to decide on the extent of the profits that need to be distributed among investors and the amount that needs to be retained by the organisation. In order to ensure business sustainability, effective financial management becomes vital. Ineffective financial decisions could lead to financial problems such as lack of liquidity, high debts, low profits, loss of investor confidence, and even bankruptcy (Issa et al., 2024). Thus, financial management assumes a strategic significance.

2.2 Capital Structure Theory

2.2.1 Definition of Capital Structure

The capital structure of an enterprise entails the proportion between debts and equities utilized by a firm in the financing process (Bui et al., 2023). This is critical since the capital structure impacts various aspects including risk, rate of returns, cost of capital, financial flexibility and corporate

worth. Too much or too little borrowing can hinder a business from deriving low-cost finances while excessive debt could lead to an increased chance of bankruptcy. Thus, firms ought to establish a capital structure which facilitates development while maintaining risk within safe limits.

2.2.2 Modigliani and Miller Theory

One of the prominent theories of capital structure is Modigliani and Miller theory. The theory proposes that capital structure should not have any impact on corporate value as long as the business environment is perfect (Brusov & Filatova, 2023). Under this condition, corporate value will only depend on the firm's earnings from operating activities and investment decisions and not on capital structure since the two financing sources provide the same returns at the same level of risks. However, practical environments have issues such as tax considerations, bankruptcy costs, etc. However, trade-off theory provides a more practical rationale. It assumes that companies seek a balance between the advantages of debt and the costs of financial distress. On one hand, debt can decrease the cost of capital through the tax deductibility of interest. On the other hand, more debt raises risks. Overleveraging could lead to higher required returns by lenders and investors, hence higher borrowing costs. Thus, according to this theory, companies should seek their optimal debt level. According to pecking order theory, companies tend to prefer internal financing, debt, and finally equity (Rodriguez, 2024). The reason is that managers generally possess more information about the firm than external investors. When issuing equity, external investors could regard it as evidence of share overvaluation. Thus, this theory emphasizes the impact of information asymmetry on corporate financing. Agency theory centers on conflicts among managers, shareholders, and creditors. Debt can serve as a managerial disciplining tool by imposing mandatory debt servicing requirements and strict cash flow management. At the same time, excessive reliance on debt might increase pressures on managers, leading to reckless behavior. Consequently, when making capital structure decisions, governance and control factors should also be considered alongside cost, return, and risk aspects.

2.3 Debt, Equity, Risk, and Return

There are two major ways to obtain long-term finance, namely debt and equity. In turn, there are significant differences between debt and equity financing in terms of risks and rewards. First, the former helps raise money without sharing ownership or management rights. At the same time, it might be more profitable than equity since creditors expect lower rates of returns from investments compared to stockholders since the latter have a higher priority in the case of bankruptcy and greater influence on firm finances. Besides, interest expenses might decrease the company's tax liabilities. Still, the use of debt entails significant financial risks as well (Bui et al., 2023). In particular, it obliges firms to make regular payments for interests or principal regardless of the state of their profitability. Moreover, the company will face challenges when trying to cover its debts when cash flows decrease. In such a way, it might experience liquidity problems, downgrading of its creditworthiness, and even bankruptcy. High levels of debt might also limit the possibility of getting new loans. Thus, debt improves returns in case of successful business operations, while it decreases the value otherwise.

Equity financing does not have fixed payments to be made at certain intervals; hence it is less risky when liquidity is considered. Equity financing can lead to a stronger balance sheet and enhanced financial flexibility. This can be helpful to organizations involved in highly dynamic or uncertain industries. Nevertheless, equity financing leads to dilution of existing ownership in the organization. In addition, earnings per share of the organization could be diluted if the equity funding does not produce enough profits. Finally, equity is costlier than debt because of the increased risks associated with equity financing. The capital structure that fits well in one situation cannot work in another situation (Handoyo et al., 2023). This is because the most appropriate combination of debt and equity will vary depending on several factors such as the industry, risk profile, interest rates, taxation policies, cash flows, capital assets composition, and management strategies. Organizations in mature stages may borrow at a high level, whereas organizations in a start-up phase in a technology-intensive industry will need more equity financing since their cash flows are unpredictable.

2.4 Investment Appraisal Techniques

Investment appraisal techniques are vital for financial managers to determine the feasibility of an investment proposal. Investment appraisal techniques play a crucial role due to the high level of

capital involved, the time horizon, and uncertainty about future cash flows. Sound investment decisions can increase a firm's profitability and shareholders' wealth, while bad decisions can destroy value.

Net Present Value, abbreviated NPV, is regarded as one of the most effective approaches for investment evaluation (Dobrowolski & Drozdowski, 2022). It determines the difference between the present value of future cash flows and the initial cost of investment. When a project has positive NPV, it suggests that the undertaking will generate wealth. The NPV method is valuable since it considers the time value of money and the creation of value. The Internal Rate of Return, abbreviated IRR, is the discount rate at which the net present value equals zero. The IRR technique provides the expected return expressed in percentage terms, facilitating comparisons (Arjunan, 2022). However, IRR has several drawbacks. For example, the IRR approach can provide misleading conclusions for investments with unique cash flows and various scales. Payback period calculates the duration taken for recovery of initial investment. This method is easy to calculate and helpful in measuring liquidity risk since it focuses on recovering the cash invested. Nonetheless, it fails to factor in cash flows beyond the payback period and also the time value of money. Profitability index ratio determines the relationship between the present value of future cash flows and initial investments (Prokopenko et al., 2023). This technique is important in situations where resources are scarce since it reveals value creation per unit of investment made. In addition, a profitability index greater than one indicates value creation by the project.

Finally, while investment appraisal techniques are helpful, they have some limitations. The techniques rely on certain assumptions regarding cash flows, discount rate, inflation, demand, competition, among other factors. As such, financial managers ought to apply various approaches along with sensitivity analysis and scenario planning.

2.5 Cost of Capital and WACC

The cost of capital means that an organization must achieve a certain return on investment in order to make its investors happy. The return is usually achieved by investing in such projects that provide returns greater than the cost of capital. Otherwise, a firm would be destroying value since the returns achieved do not cover the risks undertaken by the investors and other finance providers.

WACC stands for Weighted Average Cost of Capital. As its name implies, WACC takes into consideration both costs of debt and equity in proportion to each other (Arhinful et al., 2024). It is worth noting that WACC is widely used when assessing new investments since the discount rate used during the Net Present Value analysis usually equals to the WACC. In case the returns expected from a certain project are higher than the WACC, a company could create value. Otherwise, a project could lead to destruction of value. There is a direct relationship between capital structure and the WACC. Debt being cheaper than equity, a reasonable amount of debt might help in lowering the cost of capital, allowing the organization to maximize value by undertaking projects whose returns are higher than the WACC (Cerón et al., 2026). If the debt ratio is too high, however, it will lead to an increase in the WACC because lenders and shareholders require more return to counter the increased financial risk.

Hence, there is more to the calculation of the WACC than just a mathematical process. Financing and investment are closely linked through WACC. An organization that adopts an effective capital structure will be able to lower the WACC and undertake profitable projects with ease.

2.6 Shareholder Value and Sustainability

Maximizing shareholder value is an important consideration in finance, but it should not simply equate to short-term profit maximization. Sustainable growth, proper financing, adequate risk management, good corporate governance, and continuous investments towards maintaining competitive advantage are the factors that create shareholder value in the long run. A firm's narrow focus on maximizing its financial gains in the short term could adversely impact its value in the long term by neglecting risk management, stakeholder relations, innovation, and sustainability.

It is possible for organizations to create financial benefits through their efforts towards sustainability (Rodríguez-González et al., 2022). Investments towards improving efficiency, reducing wastage, creating good reputations, and positioning companies for upcoming changes in regulations and markets could benefit firms in the long run even if such activities do not lead to immediate gains. As such, sustainability must not be treated separately from value creation.

The contemporary organization should also consider environmental, social, and governance issues in making investment and financing decisions. The project could be viable based on its financial

profitability; however, it might lead to reputational issues, fines, environmental costs, or resistance from stakeholders, especially if it is irresponsible. In the same vein, high debt ratios might result in increased profits in the short term but decrease organizational resilience due to its susceptibility to interest rates and economic conditions (Wolf & Karszes, 2023).

Hence, financial managers need to find the right balance between maximizing shareholder wealth and ensuring sustainable financial management practices. The best financial decision is one that generates value and ensures financial stability, stakeholder confidence, and organizational resilience. This highlights that capital structure, investment appraisal, cost of capital, and sustainability have strong connections.

3. Methodology

This report applies the secondary methodology of research because the analysis is conducted in a non-descriptive way by reviewing the available literature. The objectives of applying the chosen methodology include analysing the application of theories and approaches in financial management concerning capital structure, investments' assessment, cost of capital, risks and value of businesses. Academic literature, textbooks on financial management, business case examples and financial statements from the company's annual reports will be used as the sources of information. Literature review will allow analysing the theoretical basis for decision making in financial management and provide information on practical aspects of using various financial tools in the field. The sources will be reviewed by performing thematic analysis of financial management. Key themes that will be identified as part of this process include debt and equity financing; risks and returns on investments; business value; sustainability and investment appraisal including payback period, net present value, internal rate of return and profitability index. Comparison of debt and equity financing will be performed and discussed in the paper. The role of debt finance and its influence on business value and risk will be considered. Examples of financial analysis as well as practical cases from organisations are employed in this research in order to illustrate the way in which financial techniques influence the accept or reject decision in a project. This report also provides a critical analysis of shareholder value and sustainability since modern finance management has to incorporate profit generation as well as responsibility.

There are certain weaknesses inherent in this research approach. Firstly, information that is available to the public may not be able to capture all the aspects of financial decision-making within the organisation. Secondly, investment appraisal illustrations might employ certain assumptions whereas in reality there are numerous elements like uncertainty, competition, regulation, inflation, and behavioural issues.

4. Findings

This part uses theory and techniques associated with finance management in relation to the chosen topic. In this case, the analysis is centered on the impact of capital structure and investments on the worth of the company. The results indicate that financial decision-making impacts companies through risk, reward, cost of capital, cash flows, and sustainability.

4.1 Capital Structure and Business Value

The capital structure plays a role in business valuation since it shows how the firm is financing its activities and growth. The capital structure is comprised of equity and debt, and the right combination of both will ensure that risks and costs are balanced and returns are optimized (Arhinful et al., 2024). The correct capital structure should aid the firm's growth, and a poor one can put pressure on its finance and destabilize the business.

Debt is considered to add value to business operations when used in an appropriate manner. Since it is less expensive than equity, it is able to boost the return generated for the owners by increasing their gains above the rate of return. But the disadvantage of debt financing is that it makes the business susceptible to any financial troubles as debt requires mandatory payments regardless of the revenue earned by the firm.

Equity financing helps improve the flexibility in financing as compared to debt. This is especially true for business organizations with unstable cash flow and a higher growth potential. The issue with equity financing is that it can lead to the loss of control by the current equity owners (Tarighi et al., 2022).

Capital Structure Strategy

The optimal capital structure will depend on the nature of the entity. For instance, entities that have a steady flow of cash flows, such as utility companies, will likely adopt more leverage compared to technology companies and startups whose future cash flows are not known.

Generally, business value can be maximized where financing decisions correspond with the strategic direction, risks, and investment requirements of the firm (Bui et al., 2023). There is no perfect combination of equity and debt capital structure.

4.2 Application of Investment Appraisal Techniques

Investment appraisal methods assist companies in determining the viability of projects prior to making significant investments. For instance, a business may undertake a project that involves investing £1,000,000 and yields cash flows of £300,000 annually for five years. Using a discount rate of 10%, the project can be evaluated by using the net present value, internal rate of return, payback period, and profitability index.

The net present value technique involves discounting the cash flows to their present value and comparing them with the initial investment. In this case, the project will yield a positive net present value of about £137,000, indicating that the project will add value after compensating for the minimum rate of return (Brusov & Filatova, 2023). The project is therefore acceptable according to the criterion.

The internal rate of return would be about 15%. It is greater than the discount rate of 10%. It indicates that the project yields return that exceed the minimum rate of return. Therefore, it is acceptable according to this measure. Nonetheless, if the weighted average cost of capital rises closer to 15%, the project becomes riskier.

Payback period is estimated to be about 3.3 years; hence, the organization will have recouped their investments before the project reaches the end of its life cycle of five years. It is beneficial from a liquidity point of view as the business will recoup their money reasonably quickly. Profitability index is greater than one, signifying that the project generates more benefits than its costs.

In summary, the results indicate that investment appraisal techniques enhance decision-making processes among financial managers. Nonetheless, care needs to be taken when using such tools, since they depend heavily on reliable data regarding cash flows and discount rates.

4.3 Cost of Capital and Risk Assessment

It is crucial to consider the cost of capital when evaluating investments since it determines whether a project looks appealing or not. In investment appraisal, the discount rate applied is often the weighted average cost of capital of the company. When the WACC is high, future cash flows are discounted more, resulting in a lower NPV for the project. As a result, fewer projects are accepted (Danielson, 2023). However, when the WACC is low, future cash flows are valued more highly, thus making investments more appealing.

Risk analysis is vital because future cash flows are uncertain. For instance, there could be underestimation of sales, an increase in operating expenses, rising interest rates, or changing market conditions. Neglecting these factors may cause a project to initially look profitable but eventually become unprofitable.

The use of sensitivity analysis and scenario analysis is recommended by financial managers (Sharma et al., 2022). Through sensitivity analysis, the impact of one factor on the NPV of the project is analyzed. The effects of varying levels of sales revenue or operating costs on the NPV can be assessed. Scenario analysis involves analyzing the best-case, base-case, and worst-case scenarios. Under unfavorable conditions, a positive NPV may turn out to be negative.

Consequently, financial management should not take on projects solely based on the profitability of their major forecast. Assumptions should be carefully reviewed, and the project evaluated for its potential to add value even under adverse circumstances.

4.4 Real-World Financial Decision-Making Examples

In the real world, organisations rely on financial decision making for expansion, stability, and maximisation of value (Cheng et al., 2024). Organisations borrow money to expand at low interest rates and where the expected returns on the investments are greater than the cost of servicing the borrowed money. In this case, financial decisions increase shareholder value but create financial risks since the organisation has to meet its obligations.

Other organisations raise money through the sale of shares. They do this to build their balance sheets and reduce financial stress, particularly in challenging economic times. Nevertheless, the

issuance of new shares lowers per-share earnings and dilutes ownership of shareholders in the organisation (Park et al., 2025).

Organisations can also opt not to invest in projects due to the high cost of capital. High interest rates increase the cost of capital, and this, in turn, lowers the net present value of a project.

A firm could also choose to invest in technologies, sustainability efforts, or restructuring activities to create sustainable value. Such investments would involve heavy upfront costs; however, they would bring efficiencies, cost savings, enhance reputation, and enable future competitiveness. This implies that actual finance decisions should consider not just profits, but also the effect on risks, liquidity, shareholder wealth, and sustainability.

5. Discussion

Based on the findings, it is evident that the capital structure and the investments made are directly related to the business value. The financial managers will have to make decisions about choosing either debt or equity and consider the implications that such decisions will have on the risk, cost of capital, investment performance, and sustainability of the firm.

5.1 Critical Evaluation of Debt and Equity Financing

There are merits and demerits of debt and equity financing. Debt may lower the weighted average cost of capital because it is relatively less expensive than equity. In addition, debt financing can enhance shareholder value where profits earned through investments exceed the interest costs (Arhinful et al., 2024). However, there is a problem associated with the obligation to repay the borrowed funds, especially when cash flow falls.

Equity financing offers greater flexibility in the sense that there is no need to repay borrowed money on a regular basis. Equity financing is appropriate for firms with unpredictable cash flows and those experiencing rapid growth ((Kaya, 2024). However, equity can dilute share ownership and is relatively costly because investors normally demand higher returns than creditors.

It is important for managers to strike a balance between excessive and inadequate leverage. An under-leveraged firm may be failing to capitalize on relatively inexpensive funding. On the other

hand, over-leveraging may negatively impact credit rating, financial flexibility, and the likelihood of bankruptcy.

5.2 Strengths and Weaknesses of Investment Appraisal Tools

Investment appraisal methods allow management teams to estimate the value that will be generated by a project; however, these techniques differ in their usefulness. The net present value technique is considered one of the most reliable appraisal methods since it measures the actual value generation while considering the time value of money. Nonetheless, a good prediction of cash flows and appropriate discounting are essential for calculating NPV.

The internal rate of return method helps management teams estimate how high the actual return would be; therefore, it is easily comparable to the cost of capital. Nonetheless, IRR can lead to misleading results if a project has unusual cash flows or when comparing different projects (Abdelrahman, 2025). While the payback period helps with estimating the profitability of a project, it focuses only on cash flows during the payback period.

Finally, the profitability index allows managers to estimate the value created by an investment project relative to its cost. Nonetheless, this technique cannot replace the use of the NPV method since it might ignore large-scale investments. As a result, there is no ideal technique for evaluating investments.

5.3 Risk, Sustainability, and Long-Term Value

However, such decisions should consider factors other than those associated with short-term profits. For instance, a certain decision might be quite profitable, but it is possible that the decision will pose significant environmental, reputational, regulatory, and stakeholders' risk for the organisation in question. Neglecting the aforementioned factors could lead to negative business value of the decision in spite of its initial profitability.

A sustainable financial decision making should include considering not only profitability of the financial decision but also its potential risks to the organization, such as ESG risk, ethical financing issues, proper leverage, reporting issues, and stakeholder issues, among others.

Therefore, it is important that the value created through financial decision making should not be assessed solely based on the profit made through this process.

5.4 Strategic Role of Financial Managers

It should be mentioned that financial managers act as decision makers rather than just being involved in accounting and budgeting. The responsibilities of the financial manager include selecting appropriate investment opportunities, structuring the capital, assessing risks, talking to investors, and developing long-term strategies of their organisation.

It is important to emphasise that due to the work of the financial manager, the company is able to adapt its strategy and behaviour towards the changes in the market, interest rates, investors' demands, and regulations (Nkwinika & Akinola, 2023).

In general, proper financial management ensures higher organisational value because the resources will be used for projects that yield better returns on investments compared to the rate of capital while maintaining reasonable risk.

6. Conclusion

From the findings, it is clear that capital structure and investments determine the value of a business. Capital structure affects the cost of capital, financial risk, financial flexibility, value added, and development of a business. The optimal capital structure can help in value addition by maximizing the advantages of both the debt and equity while the poor capital structure such as overreliance on debts or inappropriate equity will reduce the business value.

The process of assessing whether an investment is profitable can assist the business to predict whether the investment will create any value. NPV can be considered the best way of evaluating projects since it measures the creation of value and the time value of money. NPV alone cannot be used to measure business decisions; other methods include IRR, payback period, profitability index, and risk analysis.

As highlighted above, financial managers should also ensure that they incorporate sustainability into their value-maximizing decisions. Value maximization does not only involve maximizing financial gains for an organization. It entails making prudent financial decisions that lead to

organizational success while safeguarding stakeholder interests. This implies that the practice of finance should encompass not only returns but also sustainability and growth.

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