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MASTER THESIS

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| RIBOTOS ATSAKOMYBĖS BENDROVIŲ KAPITALO KAŠTŲ IR JUOS VEIKIANČIŲ VEIKSNIŲ ANALIZĖ | ANALYSIS OF LIMITED LIABILITY COMPANIES' COST OF CAPITAL AND ITS INFLUENCING FACTORS |
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ABSTRACT

The purpose of this research is to understand what factors and how do they affect the cost of capital of Limited Liability Companies (LLCs). Cost of capital is used by many LLCs and it has become in the one of the most significant types of measurements for businesses and it represents the overall expense incurred by a company to secure financing for its operations and growth. Trying to find the best mix of cost of capital for LLC is very important as LLCs must make appropriate financial decisions, attract investors and remain competitive in the market. This study uses a comprehensive approach which include: incorporating financial theory, statistical and graphical research and survey to better understand the LLCs' cost of capital in the example of GrandMart LLC functioning in Azerbaijan. The major components which influenced to the cost of capital were discovered and investigated. The research took into account both internal and external factors. This research also identifies how the special characteristics impact the cost of capital and its sensitivity to changes in economics, regulatory environment, technological advancement, innovations and market trends.

INTRODUCTION

Relevance of the topic. The activity of any enterprise depends on many aspects, including material ones. The factors that contribute to the production of goods and services are broadly categorized into three types: capital, natural resources (such as land) and labour resources. They are production resources and therefore, their use in production is associated with the costs that must be incurred to attract this resource (dividends, interest, wages). The comparative significance of these resources can be assessed in different ways, in particular, depending on whose position this assessment is made - the state, the enterprise, its owners, etc. As has been repeatedly admitted, financial resources play a dominant role from the position of the enterprise and therefore, it is quite natural that in financial management a special place is occupied by a section devoted to the assessment of capital and the sources of its formation.

Commercial organization that wants to finance its operations nowadays and in the future is required to have sources of funding. Taking into account how long they will be used, a business's assets and funding sources can be split into parts as either long-term or short-term. The company ought to pay expenses like dividends to shareholders, interest on bank loans and investor returns on investment when it gets funding from different sources. The percentage of funds that is ought to be paid for with a specific quantity of financial resources is considered as the cost of capital. Long-term funding sources ought to ideally be used to finance long-lasting assets, while short-term funding sources ought to be used to finance current assets. In result, the total cost of raising money is gone down.

One of the main ideas in the research of finance is the cost of capital. It is not just figuring out how much money need to be paid in cash to the suppliers of financial resources. It also gives the profitability level that the business requires to keep up with capital investments to hold its market value intact.

Due to its connection to a company's financial health, the cost of capital is very important. Profitability, income, liquidity and solvency of a business may all be impacted by how it increases and uses capital. Both internal and external stakeholders assess a company's funding sources and use the results to evaluate the financial risk associated with the business while making decisions. The percentage of a company's funds compared to its total sources of funding can be of particular interest to external parties like banks, investors and lenders as a lower percentage of equity capital increases financial risk. An internal capital structure analysis is necessary to evaluate the different options available for funding the business's operations. The key factors taken into account while making this analysis consist of the terms of borrowed funds, the cost of the funds, the level of risk and the intended use of the funds.

The novelty of the thesis lies on calculation of cost of capital and identifying the factors influencing the company's cost of capital, future research will reveal the methodological and empirical aspects.

The composition and placement of the enterprise's property in value terms and the sources of its formation as of the reporting date characterize the property and financial condition of the enterprise. The financial condition of an enterprise is determined by its ability to finance its activities at the expense of its own, borrowed and borrowed funds, their skilful placement and effective use.

The financial situation of an enterprise can be totally stable, normally stable, unstable and in crisis. The overall financial situation of a business is identified by the outcome of its operations. With the fruitful pursuance of plans for the production and sale of products, decreasing its cost, raising the mass of profits, skilful allocation of working capital, etc., the financial state of the enterprise can be upward strengthened and vice versa.

The financial condition of a company is of interest to a wide range of stakeholders, such as the management and owners of the company, investors, financial institutions, suppliers and tax authorities. These parties use the information to monitor the efficiency of the company's use of financial resources, assess creditworthiness and risk, ensure timely payments and ensure compliance with tax regulations, respectively.

To evaluate the financial health of a company, various indicators are used that reveal information about the structure and sources of the company's capital, its usage efficiency and intensity, the company's solvency, creditworthiness and financial stability.

The aim of the master thesis is to analyse the structure and cost of capital in the example of GrandMart LLC functioning in Azerbaijan.

Tasks of the thesis are the following in order to achieve the aim:

- Theoretical foundations of the structure and cost of capital;
- Exploring methodological aspects;
- Highlighting the empirical aspects;
- Analysis and results on the example of GrandMart LLC;

The subject of the master thesis is the cost of capital analysis of "GRANDMART" LLC and influencing factors.

The object of the course work is "GRANDMART" LLC in Azerbaijan.

The research question is the factors affecting limited liability companies' cost of capital.

The theoretical foundation of this research draws from the work of domestic and foreign scholars in the field of theory and structure of capital.

The empirical base of the study is represented by statistical materials characterizing the current structure of capital in Azerbaijan.

Research methods of the research: literature review, secondary data analysis, statistical analysis, graphical analysis, survey.

Limitations of the thesis is lack of information about cost of capital of LLCs in Azerbaijan. There is almost no research works conducted in this field in the country. The second limitation is difficulty in accessing the financial report about LLCs in Azerbaijan and the third limitation is the challenges to get in touch with entrepreneurs of LLCs in Azerbaijan.

The structure of the thesis. The master thesis will be composed of an introduction, three chapters split into subchapters, a conclusion, an appendix and a list of references.

Chapter 1, titled "Theoretical Foundations of Capital Structure Analysis," provides an overview of the major concepts and theories related to capital structure in corporate finance. This chapter serves as the theoretical framework for the subsequent analysis of capital structure in the context of limited liability companies. The chapter begins by defining the concept of capital structure, which refers to the mix of debt and equity financing used by a company to fund its operations and investments. It highlights the significance of capital structure decisions and their impact on the financial performance and risk profile of the company. Next, the chapter delves into various theories and models that have been developed to explain and analyse capital structure choices. The chapter also discusses the factors that influence capital structure choices, such as firm-specific characteristics (e.g., profitability, size, growth prospects), industry characteristics, macroeconomic conditions and regulatory environment. These factors are important considerations for understanding and analysing the capital structure of limited liability companies.

Chapter 2, named as "Research Methodology," gives the approach and methods used in the thesis for analysing limited liability companies' cost of capital and its influencing factors. This chapter highlights a detailed description of the research design, data collection and data analysis techniques used in the study. The chapter begins by stating the research objectives and research question that guide the study. It highlights the specific focus of the research, which is to analyse the cost of capital and its determinants in limited liability companies. Next, the chapter discusses the research design utilized in the study. It explains whether the research is qualitative, quantitative or a combination of both. It justifies the chosen research design by highlighting its suitability for addressing the research questions and achieving the study's objectives. Following the research design, the chapter provides a comprehensive description of the data collection methods. It specifies the sources of data used, such as financial statements, company reports and industry databases. It explains how the relevant data was gathered, including the time frame and

sample selection criteria. Moreover, the chapter discusses the variables and measures used in the analysis. It describes the key variables, such as the cost of capital, debt-to-equity ratio, profitability, firm size, industry type and other factors influencing capital structure choices. It explains how these variables were operationalized and measured to ensure reliability and validity. Subsequently, the chapter presents the data analysis techniques used in the study. It describes the statistical methods, econometric models, or other analytical tools used to analyse the collected data. It explains the rationale behind selecting these particular techniques and how they align with the research objectives. Additionally, the chapter addresses any potential limitations or challenges encountered during the data collection and analysis process. It discusses strategies implemented to mitigate these limitations and ensure the validity and robustness of the research findings.

Chapter 3, titled "Data Analysis" presents the findings of the analysis conducted on the cost of capital and its influencing factors in limited liability companies. This chapter provides a comprehensive discussion of the results obtained from the data analysis and their implications.

1. THEORETICAL FOUNDATIONS OF CAPITAL STRUCTURE ANALYSIS

1.1. Theoretical Foundations of the Concept of "Capital"

The concept of "capital" has its theoretical foundations in the field of economics and captures various dimensions, each with its own theoretical framework. The key theoretical foundations related to the concept of capital are as follows (Hayek & White, 2019):

- *Classical Economics*

Classical economists such as Adam Smith and David Ricardo laid the foundation for the concept of capital in their works. They viewed capital as a factor of production alongside labour and land. According to their theories, capital represents the accumulated wealth that can be used to generate income and increase productivity.

- *Neoclassical Economics*

Neoclassical economists, including Alfred Marshall and Leon Walras, built upon the classical economic theories and introduced the concept of marginal productivity of capital. They emphasized the role of capital in increasing output and believed that its value is derived from its contribution to production.

- *Marxian Economics*

Karl Marx's theories of capitalism and socialism provided a critical perspective on capital. Marx defined capital as accumulated wealth that is used to exploit labour and generate profits for the capitalist class. He argued that capital accumulation is a central characteristic of capitalism and leads to social inequality.

- *Human Capital Theory*

Developed by economists such as Gary Becker, the concept of human capital emphasizes the importance of investing in education, training and skills development and also, human capital refers to the knowledge, skills and abilities that individuals possess, which can be seen as a form of capital that enhances productivity and economic growth.

- *Financial Capital Theory*

Financial capital refers to money, stocks, bonds and other financial assets that are used for investment purposes. Financial economists focus on the allocation and management of financial capital and study factors such as risk, return and portfolio diversification.

- *Social Capital Theory*

Social capital refers to the social relationships, networks and norms that facilitate cooperation and collaboration within a society or community. Social capital theorists, such as Robert Putnam, argue that social capital has economic value and can contribute to improved outcomes in areas such as education, health and economic development.

1.2. The Main Theories of Capital in the History of Economics

First, the main theories of capital, which are reflected in the history of economic doctrines, are considered briefly.

1. The theory of capital F. Quesnay

There was a political movement in France in 18th century that marked a shift in economics, known as "physiocracy" (from Greek, meaning "the power of nature").

F. Quesnay is considered as one of the first economists in history to provide a thorough theoretical basis for the concept of capital. According to the terminology of the scientist, agricultural implements, buildings, livestock and everything that is used in agriculture during several production cycles represent "initial advances" (according to modern terminology - fixed capital). The costs of seeds, feed, wages of workers and others carried out for the period of one production cycle (usually up to a year), he referred to as "annual advances" (working capital) (McConnell & Brew, 2018, p. 178).

The merit of Quesnay also lies in the fact that he was able to convincingly prove that fixed capital is in motion along with circulating capital. The Physiocratic school came out with sharp criticism of monetarism. F. Quesnay rejected the belief that gold is the only form of wealth and that it comes from foreign trade, which were misconceptions about the concept of wealth. F. Quesnay and his colleagues believed that wealth is made up of use values. Money was assigned the role of an intermediary in circulation.

They saw the source of wealth in production and not in trade, which, in their opinion, is characterized only by the exchange of equal values (equivalent exchange). The contribution of Physiocrats is that they shifted the study of the surplus product from the exchange process to the sphere of production and laid the foundation for the analysis of capitalist production. However, the Physiocrats have a narrow perspective, by focusing only on the agricultural sector of production. Hence, the labour of farmers was considered the only productive labour.

To explain the process, the Physiocrats took such a branch of labour that "protrudes outward regardless of the process of circulation" (Alekseeva, 2017, p. 190), which they saw only in agriculture. From their point of view, industry was not a productive branch of the economy.

2. A. Smith and his theory of capital

Smith's point of view is as follows: capital as the assets used in production, from which the capitalist foresees generating income. Frugality was essential in Smith's outlook as the main driver behind capital accumulation. He found it as directly triggering the growth of capital. Corroborative frugality, he stated that savings constituted a fund supporting productive labour. Smith principally classified capital into fixed and circulating categories. He identified circulating

capital as progressively transitioning from its owner in one form and going back in another. In opposition, fixed capital is held outside the circulation process, remaining within the possession of its owners. Smith essentially associated merchant capital with working capital.

The portion of advances into initial and yearly payments was limited to agricultural capital in the Physiocratic era. Smith collected together all economic sectors in his classifications of fixed and circulating capital. But Smith implemented these portions of fixed and circulating capital incorrectly to circulation capital, which was a fault, instead, the Physiocrats linked them to productive capital. (Anisin, 2018, p.16).

The way that Smith did, it is not correct to distinguish between circulating and fixed capital on the basis of the latter's lack of circulation. By means of the separate ways, they both do. Truly, Smith compared one with another in the areas of productive capital and circulation capital rather than fixed and circulating capital. He did not correctly interpret circulation as a displacement mechanism. In result, he believed that the components of fixed capital were completely steady.

Smith made simple the issue of capital accumulation to the conversion of profit (surplus value) into higher wages. In opposite to Smith's perspective, only a division of the profit from the build-up of capital moves toward hiring more labour. The purchase of extra means of production is covered by the rest division. Smith made a conclusion that when capital accumulation results in risen wages, workers really make use of it. He concluded from this that the working class's situation would make better as capitalism gets developed (Zhid & Rist, p. 223). Smith came to an assertion that is under doubt.

3. The theory of capital by K. Marx

Usually, capital is understood as the relation of a person to his property - money, buildings, tools, etc. This relation is expressed in the fact that, for example, money is not consumed, but is used for the purpose of making a profit, in other words, an apartment in itself is not capital, it is only capital when, for example, it is rented out. Marx, on the other hand, understood capital as a relationship between the owner of property and a worker hired to work with property, money, etc. This relation, according to Marx, is nothing but the exploitation of labour. Marx has another concept of capital - self-increasing value (cost), perhaps it will be able to better clarify the essence (Chepurina & Kiseleva, 2013, p. 261).

Marx then separates capital employed and capital consumed—applied capital equals fixed + circulating capital and capital consumed equals depreciation (depreciation of fixed capital), wages, material consumption—or what economists call the cost of goods, the direct cost of production. On the one hand, we have one-time, one-time costs (capital in the usual sense), on the other hand, direct production costs for the production cycle. It is with this concept that Marx

operates in the first volume of “Capital”. As you can see, Marx often confuses these two concepts: applied, consumed and here and there - capital, although in one case - one-time and in the other - current costs.

Marx also introduces the concept of the organic composition of capital. According to Marx, capital is divided into fixed and variable. Variable capital, Marx called the part that is intended for wages (wage fund), constant capital, therefore it is everything. Here Marx was not even embarrassed by the fact that constant capital was also understood as part of the circulating capital (for example, the consumption of materials in one cycle), Marx argued that constant capital does not change its value in the production process, that is, they simply transfer their value to the product and how much they decrease, so much is added to the value of the product.

Since in this case it is impossible to assume consumer value, we conclude that, according to Marx, depreciation costs are included in the exchange value, in the price of the product. Variable capital "reproduces its own equivalent and moreover, excess, surplus value" (Zhukov, 2016, p. 48). Surplus value can be boldly equated with profit and what do we get? Has capital changed because some part of it has made a profit? It is obvious that the profit itself will not be added to the capital.

Marx, on the other hand, has changed that part of the capital that goes to pay for labour, “that part that has been turned into labour power” (Plotnitsky & Tur, 2017, p. 273), but labour power has not increased from profit and the wage fund has not increased by profits, otherwise the workers would have received the full product of their labour.

Marx argues as follows: first there was capital, then, when the product was made, surplus value appeared. Obviously, Marx not only mixes capital with production costs, but also with value or price, $production\ costs + profit = price$. Marx concludes from this reasoning that capital is a self-increasing quantity.

It should be remembered that capital was written in order to prove the main thesis of the Manifesto - the thesis that the exploitation of labour by capital lies in the nature of capitalism, i.e. changing the status quo in an evolutionary way is impossible. To do this, it is necessary to prove that all profit is generated by living labour, while capital plays a passive role and does not generate surplus product. Therefore, he allocates the wage fund (variable capital) and proves the increase of variable capital in the process of production.

4. Neoclassical school.

A. Marshall's theory of capital was formed in the 90s of the 19th century after the publication of A. Marshall's book "Principles of Economics" (1890).

Neoclassical theory explored the market economy during the period of free competition. He combined the ideas of classical political economy with the ideas of marginalism. Marshall

understood the emergence of limiting analysis not as a revolution in science, but as the result of its evolution. After utility was combined with social costs, a general theory of comparing results and costs was created; the so-called second classical situation arose. The neoclassical school dominated until the 1930s.

First of all, it is necessary to pay attention to the peculiarities of the methodology of neoclassical analysis. In all previous theories, the source of value, the absolute law of its formation, was distinguished first of all. For example, value was derived from labour costs or production costs or from marginal utility. Neo-classicists move on to functional theory, where there is no place for absolute categories, they are all considered relative. Economic phenomena are analysed not according to the principle of movement from deep causes to superficial phenomena, but according to the principle of interdependence and mutual determination (the principle of relativism). Marshall wrote: "We could equally argue about whether value is regulated by utility or production costs, as well as about whether a piece of paper cuts the upper or lower blade of the scissors" (Alekseeva, 2017, p. 310).

A number of economists, like J. Robinson and R. Dornbusch, look at capital as currency, an intrinsic commodity within the business realm.

Even in modern times, the issue of giving a definition "capital" persists, with contemporary economics lacking a globally admitted, flawless description. As per American scholars (H. Anderson, D. Caldwell, B. Needles), capital concretizes the economic resources available to a company's owner, embracing the entirety of monetary values (including cash and buyer debt obligations), tangible assets (such as land, buildings and equipment) and intangible assets represented by rights (such as patents, copyrights and trademarks). (Zhid & Rist, 2019, p. 162).

This definition is somewhat subjective, since it is devoid of the most important thing that characterizes the concept of "capital". First, it ignores the natural energy that provides the creation of life's blessings. Secondly, human abilities that actually create the labour process as benefits that form capital are also not considered.

All perspectives on capital share one common understanding: capital is related to the ability to produce income. The capital of an enterprise is one of the main factors of production created by a person in order to produce other goods and services with its help. The word "capital" comes from the Latin word "capitalis", meaning principal or dominant. Also, the term "capital" from the German "kapital" is translated as the main property, the main amount. Having studied and systematized the definitions of capital formulated by representatives of various economic schools, we can give the following definition of this economic category: "capital is an economic resource of long-term use, which is a set of material values and funds necessary for

the implementation of economic activities, which is at the disposal of an economic entity and has ability to make a profit" (Syroezhin, 2014, p. 174).

Capital means a collection of financial assets accumulated through savings, existing as either cash or tangible items. Owners may invest it in the economy as a means for production and income generation. Its role within the economy bounds up with market principles and is impacted by elements as time, risk and liquidity.

1.3. Essence and Cost of Capital of an Enterprise (LLC)

For any business to operate, it requires funding sources, namely capital. According to Blank I.V., capital signifies an accumulation of economic advantages obtained through savings, encompassing cash and tangible assets. Owners employ this in the economic cycle to produce income, serving as an investment resource and a production factor. Its application in the economy aligns with market basics and connects with elements like time, risk and the ease of asset conversion to cash. (Blank, 2014).

Table 1 shows the classification of capital according to the main features.

Table 1.

Classification of the Capital of the Company

| Classification Sign | Types |
|--|--|
| By property title | Equity; debt capital |
| By groups of sources of attraction | Capital raised from external sources; Capital raised from domestic sources |
| By nationality | Foreign capital; national capital |
| By form of ownership | Private capital; state capital |
| By organizational and legal forms | Share capital Equity capital Individual Capital |
| By natural-material form | Capital in cash Capital in financial form Capital in material form Capital in non-material form |
| By time period | Long term capital Short term capital |
| By area of use | Capital used in the real sector Capital used in the financial sector |
| By directions of use | Capital used as an investment resource Capital used as a production resource Capital used as a credit resource |
| According to the degree of use in the investment process | Initial investment capital Reinvested capital Disinvested capital |
| By the features of use in the production process | Fixed capital |
| By risk level | Working capital Risk free capital Low risk capital |

| | |
|--|--|
| | Medium risk capital High risk capital |
|--|--|

Source: Alekseeva, 2017.

Most often, when analysing the capital structure, a classification is used according to the title of ownership of the formed capital, i.e. division into equity and debt capital. Equity includes equity capital and deferred earnings (equity funds and retained earnings). The main elements of borrowed capital include bank loans and bonds issued by the enterprise. Attraction of this or that source of financing of funds entails certain costs. For equity, such costs are dividends paid to shareholders, for borrowed capital - interest on bank loans (Georgakopoulos et al., 2012).

Additionally, consideration should be given to the categorization of capital based on duration. Kovalev V.V. shows the origins of long-term financing as profit, the securities market, the banking system and the budget. Short-term funding primarily originates from accounts payable, stemming from ongoing transactions and settlements with the company's counterparts. Long-term resources come from investors and lenders, while short-term ones come from creditors. (Kovalev, 2012).

Table 2 presents a comparison between equity and debt capital. A rise in the proportion of equity capital diminishes financial risk. The earnings of equity capital owners correlate directly with the company's financial performance. These owners hold the entitlement to receive profits and have a stake in satisfying claims if the company faces bankruptcy. Additionally, equity capital owners possess the right to engage in company management, a distinction from debt capital owners.

Table 2.

Comparison of Equity and Debt Sources of Financing

| Comparison Feature | Equity Capital | Debt Capital |
|--|--|--|
| The right to participate in the management of the enterprise | Got a right | No right |
| Impact on financial risk | Increasing the share in the structure reduces financial risk | Increasing the share in the structure increases the financial risk |
| The right to receive profit | On a leftover basis | First priority |
| Order of satisfaction of claims in case of bankruptcy | On a leftover basis | First priority |
| Deadlines for payment and return of capital | Not definitely defined | Defined by the loan agreement |
| Direction of funding | Long term assets | Short-term assets |
| Impact on income tax | There is no possibility to | There is an opportunity to reduce |

| | | |
|--|---|--|
| Sources of financing | reduce income tax by attributing financial expenses to costs Internal and external sources | income tax by attributing financial expenses to costs External sources (except accounts payable) The owner's income is not related to the financial result |
| Relationship between the income of the owner of capital and the profitability of the company | The owner's income is related to the financial result | |

Source: Brigham & Gapensky, 2004

Table 2 shows that the capital structure of an enterprise has a direct impact on the results of its financial and economic activities. The proportion of borrowed and invested capital is a critical metric that measures the risk level associated with investing in a particular company.

1.4. Analysis of Models for Estimating the Cost of Capital

In modern conditions, the configuration of capital significantly impacts a business's financial condition, affecting solvency, liquidity, proceeds and profitability. New capital structure theories encompass a wide range of methodologies to optimize this factor. The Capital Asset Pricing Model (Jack Trainer, William Sharp, John Litner and Jan Mossin) stays a primary instrument for assessing an organization's capital expenditure. However, issues surface with the Capital Asset Pricing Model in emerging financial markets due to difficulties in pinpointing risk-free returns, market risk premiums and beta coefficients utilizing accessible local market data. This trouble stems from low possession fluidity and inadequate data within these markets.

Several scholarly works provide evidence against the suitability of employing the CAPM model in emerging markets. These markets possess distinct risks associated with particularities in government economic and business policies. These risks, reflecting state policy nuances, cannot be mitigated through global investor capital diversification. (Estrada J., 2002; Teplova & Selivanova, 2007).

Beckert and Harvey consider it necessary to take into account the temporary degree of variability of the integration of the local market into the global financial market when calculating the required return, in accordance with which approaches to assessing developed and emerging markets should be different. A number of papers argue that the choice of a model for estimating the cost of equity should also take into account the level of integration into the global capital market (De Swaan & Liubych, 2003).

The Godfrey-Espinosa model computes the beta coefficient and market risk premium by incorporating local market data, integrating the country risk premium (CRP) and including an

adjustment factor (R²) that links the company's performance in the local market to the fluctuations in the country risk premium. (Godfrey & Espinosa, 1996).

Despite the variety of cost of capital models, they can be conditionally divided into two types - those based on the CAPM model and those based on other assumptions rather than the CAPM model.

Sharpe's and Litner's (Sharpe and Lintner, 1965) CAPM model was the first tool for estimating the cost of equity, showing the relationship between company returns and market index returns.

For the CAPM model to be applicable, the following conditions must be met, according to Sabal (Sabal, 2004):

- Expected utility maximizing investors are risk-phobic,
- There is a risk-free rate in the market,
- The market has a market portfolio,
- There are no transaction costs,
- There is no information asymmetry,
- The distribution of asset returns is normal.

The CAPM model has been repeatedly tested in emerging markets. The explanatory power of the model, as a rule, turns out to be low. So, for example (Sehgal S., Balakrishnan, 2013), using the example of companies operating in India from 1996 to 2010, tested the CAPM model separately for each portfolio formed at the intersection of the company size and the B / M indicator. The authors concluded that this model does not explain the formation of cost of capital for some portfolios. The low explanatory power of this model is also evidenced by a study by (Kim et al., 2012) on the example of South Korean companies in the period 1990-2009.

Constraints in using the CAPM model in practical scenarios have prompted adaptations of this model. These adaptations hinge on the level of advancement of the local market and its integration within the global market.

O'Brien and Stulz (O'Brien, Stulz et al., 1999) recommended adopting a global model to approximate the cost of capital that utilized global market-based ROR as a benchmark. Nevertheless, this model requires that markets must be free, efficient also it must be transparent with respect to cash flow management, transaction costs and legal restrictions. However, these are not always possible in developing capital markets. Therefore, the model offers a limited explanation for companies in these markets (Hakim et al., 2015). The study considered non-financial firms in China, India and South Africa over the period of 2004 through 2013 and utilized MSCI World Index as a worldwide baseline. Explained ability of the model ranged between 5% and 12% in the case of China and 16-48% in the case of India and South Africa

An alternative to the poorly integrated global model could be a local CAPM, where the market index represents the local index's performance and the risk-free rate mirrors the local market rate (or the global market's risk-free rate adjusted for the country's premium). However, in underdeveloped markets, the reliability of government bonds as a risk-free tool and the challenge of accurately computing beta due to limited trading history pose difficulties in applying this model. Nevertheless, the explanatory power of the model in the formation of equity costs due to the use of local indicators should be higher than in the case of global CAPM. This conclusion is confirmed (Hakim et al., 2015). The authors found that the explanatory power of the model in emerging markets varies for each country - for China from 55% to 85%, India from 40 to 86%, South Africa from 16 to 75%, which significantly exceeds the explanatory power of the global CAPM for the same the sample of companies.

When testing alternative scenarios, (Pereiro, 2001) suggests favoring the hybrid CAPM and the Godfrey-Espinosa model (Godfrey and Espinosa, 1996). This hybrid model incorporates the determination coefficient from the regression of local market volatility and shifts in country risk. Additionally, it adjusts the beta coefficient, which indicates the local market index's responsiveness to the global one. However, due to the inconsistent beta relationship of companies in emerging markets with their global market counterparts, the model's applicability in underdeveloped markets is restricted.

The Godfrey-Espinoza model makes it possible to take into account the risks of emerging markets - political and monetary nature, by adjusting the beta coefficient for the volatility of the local market's profitability in relation to the volatility of the global market's profitability. When using this model, there is a risk that the assessment of the cost of equity is inseparable for each particular company from the entire market as a whole. On the other hand, the above risks for emerging markets are an important parameter for investors diversifying their portfolio. Therefore, this model can rather be a general guideline for an investor who is considering not a specific company, but the possibility of investing in a particular market. The importance of considering political risk by an investor when assessing the cost of capital is evidenced by a study (Bekaert et al., 2015) on companies in 20 emerging markets over the period 1994-2009.

With the practical impossibility of meeting CAPM conditions, especially in developing countries, alternative methods for estimating the cost of capital have been developed. For instance, DCAPM (Estrada, 2000) only considers investors' reactions towards decline in returns. This model has an advantage as it considers the non-normal distribution commonly occurring in these emerging markets. It also considers the behavior of investors knowing that they respond to stock price drops more aggressively rather than increase in valuation. In the research of (Tahir et

al., 2013), was noted that during 2000 and 2010 the DCAPM outperformed CAPM in emerging markets in case of Pakistan.

The Erb-Harvey-Viskanta model (Erb, Harvey, Viskanta, 1996) proposes to take into account the country's credit rating. However, this model does not calculate the cost of capital for each company but gives an overall indicative for the entire country. Similarly, the country's rating, expressed in the form of the numerical figure, is arbitrary. However, incorporating this risk into emerging markets helps investors to better assess the risk of investing in a particular country. (Almahmoud, 2014) demonstrates that investors' decisions are influenced by country's credit rating as evidenced in the Saudi Arabian market between 2005 and 2012.

Finally, it is worth mentioning the arbitrage pricing model, where several factors determine the profitability of a company (Ross, 1976). The main issue in this model remains the inclusion of "correct" factors that will not be related. This conclusion is confirmed (Geambasu et al., 2014) using the example of Romanian companies operating in the period 2002-2010. A number of macroeconomic factors were included in the model. Comparing the results of testing the model with previous studies of relevant factors affecting the cost of equity, the authors conclude that there are Romania-specific factors that determine the profitability of a company.

Fama and French (Fama and French, 1992) introduced a three-factor model that incorporates size and growth rate premiums, presenting a novel valuation approach. This model has undergone multiple assessments using data from both emerging and established markets. Presently, among various pricing models, the Fama and French model stands out for its superior capability to explain disparities in companies' cost of equity capital.

Numerous studies support the presence of a size premium within emerging markets. For instance, it was observed that the Chinese companies between 1999 and 2012 and noted a more pronounced impact of the size premium during periods of credit restriction policies (Hilliard and Zhang, 2015). Similar findings regarding this premium in the Chinese market were identified (Chen et al., 2015). Additionally, examining companies in West Africa identified a positive correlation between companies' size and their profitability (Acheampong et al., 2014).

As for the existence of a B/M premium in emerging markets, not all research in emerging markets confirms it. For example, Hilliard and Zhang (Hilliard and Zhang, 2015) deny the existence of a premium in the Chinese market during the period 1999-2012. (Chen et al., 2015) also come to the insignificance of the premium for the company's growth rate by analysing Chinese companies in the period 1997-2013.

Other than company size and the B/M ratio, other variables that significantly affect companies' profitability include. An independent examination of the well-known Fama and French three-factor model along with the same model including global market returns (Hakim et

al., 2015). China, India and South Africa are the three countries that they use non-financial companies as the sample. The authors find out their model is better for explaining small and midcap portfolios than CAPM in their first test.

In the second case, the significance of the global index depends on the country in question. So, in the case of China, it is insignificant. For India and South Africa, its significance depends on the portfolio in question. Thus, the authors conclude that China's local market index is able to take into account the risks inherent in the global market. This conclusion is confirmed by Dash and Mahakud (Dash S. R., Mahakud, 2015) on the example of companies operating in India in the period 1995-2012, which include the company's liquidity indicator in the analysis. The same conclusion is reached when additional factors were included in the equity cost analysis model for Chinese companies - the ratio of cash flow to market capitalization and the ratio of profit to capitalization (Cakici et al., 2015).

However, when new variables are added to the model, it is necessary to figure out what features contribute to improving the model's quality, not because of the increased number of explained variables, but because of how much effect they have themselves. The three factor model may be as powerful in explanation as adding the new variables would make the model. Walkshäsl and Lobe (2014) add also size, B/M ratio and investment change in relation to assets and the profit-to-assets ratio. They study firms within a set of emerging markets, examining data from 1982 to 2009. The authors conclude here that profitability doesn't help much to figure out the cost of equity. The marginal premium for investment change compared to assets also appears insignificant.

Thus, the analysis of empirical studies indicates that the Fama and French model remains the preferred method for estimating the cost of equity, since among other pricing models it has the greatest explanatory power.

1.4.1. Capital Assets Pricing Model – CAPM

A widely used financial tool for predicting the expected return on investment depending on systematic risk is known as the Capital Asset Pricing Model (CAPM). It provides a framework for calculating the appropriate expected yield rate for an asset, considering the change of the asset price with market fluctuations.

CAPM depends on the assumption that an investor would require higher return for assuming higher risk. It estimates the necessary return rate taking into account of the risk-free rate of return, expected market portfolio return and a systematic risk or asset beta. The importance of each part of the capital structure. The most commonly used approach for calculating the cost of capital is the CAPM introduced by W. Sharp and J. Litner in 1964. The

cost of capital model assumes that it is based on the market rates together with the amount of risk associated with a company's investment. In simpler terms, the equity's return rate is calculated using the following formula: (Kovalev, 2004):

$$Re = Rf + \beta(Rm - Rf) \quad (1)$$

Where Re is the required return on capital,

Rf is the return on risk-free assets,

β is the coefficient of asset sensitivity to changes in market returns, expressed as a covariance of the asset's return with the return of the entire market in relation to the variance of the return of the entire market,

Rm is the expected return of the market portfolio,

$(Rm - Rf)$ is the risk premium for investing in shares.

The CAPM assists the investors in determining if a certain investment pays fair compensation for the respective risks. Therefore, if the computed expected return by means of CAPM turns out greater than the real expected return, such asset can be labeled as an underpriced one which is a promising investment option. However, in another case, where the actual expected return is much less than the expected, the asset is considered undervalued.

Despite many shortcomings and critics of the CAPM, it is still used as one of the models to estimate cost of capital and price of financial assets especially in the areas of portfolio management and assets analysis.

1.4.2. Gordon Model

The Gordon Model, also termed the Gordon Growth Model or the Dividend Discount Model (DDM), is a valuation technique used to measure the inherent worth of a stock or company by considering its forthcoming dividends. This model finds extensive application in fundamental analysis and stock valuation.

It operates on the premise that a stock's value is reliant on the present value of its future dividends, assuming that investors assess a stock's worth based on the income it produces in the shape of dividends. Originating from the concepts proposed by American economist Myron Gordon in 1962, it stands as a variant of the dividend discount model.

The dividend discount model and the Gordon model are based on the following simplifications:

1. Market capitalization rates are equal at any given time, i.e. investors always value the risk associated with a given stock in the same way;
2. The flow of cash payments is an endless stream of dividends;
3. The growth rate of annual dividend payments does not change indefinitely;

4. The firm pays dividends regularly.

Thus, Gordon obtained the formula for the present value of a share (McConnell & Brew, 2018):

$$PV = P_0 \frac{D_0 \times (1+g)^1}{(1+k)^1} + \frac{D_0 \times (1+g)^2}{(1+k)^2} + \frac{D_0 \times (1+g)^3}{(1+k)^3} \quad (2)$$

Where,

D_0 is the amount of dividends paid per year;

g is growth rate of annual dividend payments;

k is market capitalization rate.

Gordon's model has rather rigid restrictions, so its use is limited. The model can be applied by companies with stable growth rates and companies whose growth rates are equal to or lower than the nominal growth rate of the economy. Also, such conditions as a large market capacity, stability of supplies of raw materials and materials, durability of the technologies and equipment used, access to financial resources and stability of the economic situation must also be met.

1.4.3. Arbitrage Pricing Theory – APT

The Arbitrage Pricing Theory (APT) is a financial framework utilized to forecast the expected return on an asset by examining its connection to various risk factors. It was formulated as a substitute for the Capital Asset Pricing Model (CAPM) and strives to offer a more practical and adaptable method for determining asset prices.

The APT argues that there are various systematic risks affecting expected return besides just market risk, as implied by the CAPM. Such features comprise of macroeconomic measures, industry-specific elements, interest rates, inflation rate, among the other market variables. The arbitrage pricing model introduced by S. Ross in 1976, unlike CAPM, requires less assumptions and may be taken as a reality-related theory. In this model, investors are assumed to enhance their portfolios' returns without a proportional jump risk, taking advantage of arbitrage or risk free profits across same asset prices. That is buying a security above its sale and simultaneously selling a security below its purchase.

The value of an asset according to the arbitrage pricing model is determined by the formula (Anisin, 2018):

$$R_e = R_f + b_1 F_1 + \dots + b_i F_i \quad (3)$$

Where,

b_i is the sensitivity of the asset to the i risk factor;

F_i is expected premium for the i risk factor;

i is the number of considered risk factors.

The advantage of this model is its multifactorial nature, which makes it possible to assess the influence of several factors on the stock price. At the same time, this limits its practical use, because the opinions of researchers differ in determining the factors for this model. The choice of one or another factor will be quite subjective and will depend on the goals pursued by the investor and on the type of company. For example, the company *Salomon Brothers* uses the following factors:

- GDP growth rate;
- Interest rate;
- The rate of change in oil prices;
- The growth rate of turnover spending;
- Inflation.

Next, estimating the total cost of a company's debt is considered. The total cost of a company's debt obligations is determined by the formula:

$$R_e = R_f + DM \quad (4)$$

Where,

DM is the debt margin to cover the risk of default.

Debt margin is the difference between the yield to maturity of a government bond and a listed corporate bond with a comparable maturity.

The debt margin can be computed by combining a nation's sovereign default spread with the company's distinct margin. A nation's sovereign default spread represents the gap between the yield on its dollar-denominated government bonds and the yield on equivalent maturity US Treasury bonds. The individual margin for a business is derived from published or synthesized credit ratings.

Investors are assumed to be risk averse, which means that they would demand additional returns if they are exposed to the factors identified by the APT. The betas are simply the sensitivity coefficients expressed as the amount of an asset's return is predicted to move as a result of an individual risk factor.

The APT includes several variables and measures the balance between risk and return of various assets. This allows for a more in-depth analysis of different risks that shape asset prices and is most useful when evaluating assets specific to certain industries or sectors.

Nonetheless, the weaknesses associated with the APT cause poor estimates and precise depiction of appropriate risk factors. It is important to analyze and consider the unique attributes of an asset as well as the prevailing market conditions and select the appropriate number and factors for this. The latter is based in a belief that there are no arbitrage opportunities in the market.

1.4.4. Weighted Average Cost of Capital – WACC

The determination of a company's average financing cost involves a financial measure termed the Weighted Average Cost of Capital (WACC). It signifies the minimal rate of return essential for a company to satisfy both its investors and creditors.

The WACC accounts for the ratio of debt to equity used by the company and the expenses linked to each capital type. This metric is computed by assigning weight to the cost of each capital component based on its relative contribution to the company's overall capital makeup.

The Weighted Average Cost of Capital stands as the fee for using capital, serving as the discount rate or time value of money utilized to convert forthcoming cash flows into their present value for all capital providers.

The general formula for the weighted average cost of capital is:

$$\text{WACC} = \sum_{j=1}^n r_j \times d_j \quad (5)$$

Where,

r_j is the cost of the j source of funding;

d_j is the share of the j source in the total amount of funds.

But the following formula is more commonly used (Blank, 2014):

$$\text{WACC} = r_d \times (1 - t) \times \left(\frac{D}{D+E}\right) + r_e \times \left(\frac{E}{D+E}\right) \quad (6)$$

Where,

r_d is the value of the company's liabilities;

r_e is the cost of capital;

D is the market value of the company's debt;

E is market value of capital;

t is income tax.

The WACC indicator characterizes the level of expenses of the enterprise for the opportunity to use financial resources on a long-term basis. The WACC value varies by industry, so there is no standard value for this value. However, when considering the WACC indicator, its decline will be considered a positive trend.

Every business aims to enhance its value. An optimal mix of equity and debt, referred to as the optimal capital structure, establishes equilibrium between financial gain and stability, ultimately optimizing the company's market value. Hence, a primary objective of financial

management is to oversee the enterprise's capital structure and attain the ideal mix of financing sources.

1.4.5. Three-factor model by Fama and French

The Fama and French three-factor model emerged in 1993 as an expansion of the Capital Asset Pricing Model (CAPM), addressing the issue of its limited predictive capability.

During the 1990s, Fama and French conducted an extensive investigation examining the influence of fundamental value and company size on forthcoming returns. Their research involved historical stock data spanning from 1963 to 1990, focusing on stocks traded on the NYSE.

This exploration revealed compelling trends. Stocks with greater intrinsic value (measured by the B/P ratio, the inverse of the conventional P/B ratio) demonstrated an average return of 21%, contrasting with the 8% return seen in overvalued stocks of larger corporations (growth companies). Notably, undervalued companies that yielded additional profits exhibited lower market risk (beta coefficient), whereas shares of larger firms displayed higher market risk.

In addition to market risk, the model began to additionally take into account two more criteria that determine future profitability: company size and industry specifics.

The formula for calculating the 3-factor model of Fama and French is as follows:

$$r = \gamma + \beta(r_m - r_f) + s_i \cdot SMB_t + h_i \cdot HML_t \quad (7)$$

Where,

r is the future return on the asset;

r_f is the risk-free return. It is calculated as the yield on government bonds with the maximum degree of reliability;

r_m is the return of the market portfolio (average market return);

SMB_t is an indicator reflecting the size of the company (the difference in returns between the weighted average portfolios of small and large market capitalization.);

HML_t is an indicator that reflects the undervaluation of a share (the difference between the returns of weighted average portfolios of shares with large and small ratios of book value to market value: B / P - the coefficient inverse to the classic - P / B);

β , s_i , h_i - coefficients that indicate the influence of the parameters r_i , r_m , r_f on the profitability of the i asset;

γ is the expected profitability of the asset in the absence of the influence of 3 risk factors on it.

The model showed that future returns are related to additional factors: the size of the company and its intrinsic value.

The model showed stable predictive power in various markets: USA, Brazil, Asia, Europe.

1.4.6. Erb-Harvey-Viskant Model

The model of K. Erb, R. Harvey and T. Viskant (EHV) focuses on country credit ratings, which, according to the authors, are decisive in the formation of the required return in developing countries. The authors propose to evaluate the marginal required return (lower limit) of investors in emerging markets by regression dependence relative to the constructed credit rating of the country. This is especially true for countries with a weak stock market that does not allow the use of models within the framework of the CAPM. Another feature of the EHV model is the assumption that emerging markets are segmented. The authors propose their own methodology for constructing the rating, which takes into account 5 financial, 13 political and 6 economic risk factors of the country. The scores obtained for each factor form the country's composite rating (Country Credit Risk - CCR) and have a certain correspondence with the recognized ratings of agencies (for example, S&P). CCR is a country risk score constructed by the authors that take into account political, economic and financial risks (Erb et al., 1996).

Traditionally, the following factors that form the country risk are taken into account:

- Risk caused by political and social conflicts;
- Risk of expropriation;
- The possibility of barriers to the export of capital and money;
- High probability of currency depreciation;
- The risk of non-payment of government obligations (debts);
- The risk of hyperinflation.

The Erb, Harvey and Viskant (EHV) model focuses on the political risks of developing countries, which, according to the authors, are decisive in the formation of the required return. The authors propose to evaluate the marginal required return (lower limit) of investors in emerging markets by regression dependence relative to the constructed country rating. The key assumption of the EHV model is the segmentation of emerging markets (the presence of barriers to the movement of capital).

Denoting the credit rating through CCR, the main idea of the model is reduced to the following relationship:

$$k_{t+1} = \gamma_0 + \gamma_1 \times \ln(CCR_t) + e_{t+1} \quad (8)$$

Where,

γ_0 and γ_1 are the calculated coefficients of the regression equation;

e_{t+1} is free member.

$\ln(CCR_t)$ is the natural logarithm of the country's credit rating value determined by the authors in year t.

For example, when analysing 135 countries over a number of years, the authors estimated the following regression:

$$k - k_f = b \times (a_0 + a_1 \times \ln(CCR_t)) + e \quad (9)$$

Where,

$k - k_f$ is market risk premium, i.e. the average risk of owning equity capital;

b, a_0, a_1 are calculated regression parameters.

The risk premium estimates obtained by the authors: $a_0 = 53.17$, sensitivity coefficient $a_1 = -10.47$. The value of the coefficient a_1 is negative, because a higher credit rating guarantees a lower return.

The natural logarithm is introduced to reflect the non-linear dependence of return on credit rating - at low ratings, the risk premium increases significantly. According to the authors, the level of the country's credit rating explains 16% of changes in the average yield and up to 40% of the yield volatility, which is much more significant than the dividend yield, which in some cases is chosen by practitioners as an approximate estimate of the required yield.

Thus, the EHV model allows in some cases to estimate the required return on equity, but does not take into account the psychological factors of risk perception. An alternative is the DCAPM model.

1.5. Factors affecting limited liability companies' cost of capital

The cost of capital for limited liability companies (LLCs) is affected by different factors that impact their ability to raise necessary for entity funds and the associated costs as well. The most important key factors affecting the cost of capital for LLCs include:

Risk and Return Expectations

The level of risk that is connected with an LLC's operations and the possible return on investment expected by investors significantly impact the cost of capital. Higher-risk ventures or industries may require higher returns for their higher risk bearing which may lead to a higher cost of capital.

Analysing risk and return expectations in limited liability companies (LLCs) includes: assessing the potential risks associated with investments and the expected returns that can be achieved. LLCs are types of business entities which offer limited liability protection to their owners and at the same time they allow management to be flexible. The key points to consider regarding risk and return expectations in LLCs are the following:

- Risk Assessment

- Return Expectations
- Diversification
- Investment Strategy
- Due Diligence

Conducting thorough due diligence is one of the most important factors during investment in LLCs. This includes analysing and interpreting the financial statements, understanding the company's business model, assessing the management team's experience and track record as well as evaluating the competitive landscape. This process helps investors to make a little prediction and make an informed decisions about the risk-return profile of their investment.

It should be noted that risk and return expectations can be significantly different among different LLCs and individual investors. Each investment opportunity should be carefully evaluated based on its unique characteristics, industry dynamics and market conditions. Professional advice from financial advisors or consultants with expertise in LLC investments can also provide valuable and important insights into risk assessment for an investor to understand the return expectation (Sivarajan, 2019).

Debt-to-Equity Ratio

The proportion of debt and equity financing in an LLC's capital structure affects its cost of capital. Higher debt levels can heighten risk perception, resulting in increased borrowing expenses and subsequently raising the overall cost of capital.

The debt-to-equity ratio is a financial measurement for quantifying the relationship and correlation between a company's debt (liabilities) and its equity (owners' or shareholders' equity). It offers the vision of condition of the capital makeup and financial leverage of a company, includes LLCs. Significant aspects to note concerning the debt-to-equity ratio in LLCs include the following: (Kurniawan, 2021):

- *Definition*

The debt-to-equity ratio can be easily calculated by using the formula (dividing an LLC's total debt by its total equity). The debt segment typically includes both long-term and short-term liabilities like bank loans, bonds and different forms of debt-based funding. Whereas, equity signifies the investment made by the company's owners (shareholders), accumulated loss or retained earnings and contributed capital.

- *Capital Structure*

The debt-to-equity ratio can depict the proportional mix of debt and equity funding utilized by an LLC for its operations and expansion. A high debt-to-equity ratio show a larger portion of debt funding and smaller equity funding, also signaling increased reliance on

borrowed resources. While, a lower ratio indicates a larger proportion of equity funding and also a greater dependence on the equity funding like (capital contributed by the owners).

- *Financial Risk*

The debt-to-equity ratio can show the level of financial risk associated with an LLC. Higher debt levels increase the company's financial liabilities, such as interest payments and principal repayments, which can negatively affect its cash flow and profitability and may create serious problems with going concern principle. A company with a high ratio may face a greater risk of default or financial distress especially if the company struggles to generate enough cash flow to meet its debt obligations.

- *Leverage and Return*

Using debt funding can enhance LLC owners' returns when the return on investment exceeds the borrowing cost which is also known as a financial leverage. But still, excessive leverage can also create issues during times of weak performance or economic downturns, increasing the risk to owners' of equity.

- *Industry Norms*

The debt-to-equity ratio can vary across industries and will not be the same in different sectors and industries, some industries usually carrying higher debt loads due to their capital-intensive nature or the availability of favourable borrowing conditions. Comparing an LLC's debt-to-equity ratio to industry benchmarks can provide insights into its capital structure and financial health in comparison with different companies in the same sector.

- *Risk Appetite and Growth Objectives*

The normal debt-to-equity ratio for an LLC depends on factors such as its risk tolerance, growth targets, market dynamics and especially competitors dynamics and cash flow generation capacity. Some LLCs may prioritize low levels of debt to minimize their financial risk, while others can strategically leverage debt to fund the company expansion or take advantage of beneficial investment opportunities.

Creditworthiness and Financial Performance

An LLC's creditworthiness and financial performance significantly influence the cost of capital. Strong financial health, continual profitability and a favourable credit rating given by S&P, Moody's or Fitch can lead to decreased borrowing expenses and a decreased cost of capital. (Yuryevna & Anatolyevna, 2021).

Creditworthiness and financial performance are one of the most important factors for limited liability companies (LLCs) that can affect their ability to obtain borrowing and also impact their overall financial health. There are some key considerations below which cannot be ignored when assessing the creditworthiness and financial performance as well as health of

limited liability companies (LLCs). These factors are very important and should be considered during making an important decision.

- *Creditworthiness*

Assessing an LLC's strength and capacity to cover its financial obligations and repay borrowed funds is known as creditworthiness. If the user wants to find out the approximate level of risk involved creditors and lenders evaluate its creditworthiness. Also some aspects that have an impact on creditworthiness include:

- a. Financial Statements*
- b. Business History*
- c. Credit History*
- d. Collateral and Guarantees*

- *Financial Performance*

The financial performance of an LLC is one of the most significant indicators of its overall health and can influence its creditworthiness and major factors that can affect the financial performance include:

- a. Revenue and Profitability*
- b. Cash Flow*
- c. Liquidity*
- d. Debt Service Coverage*
- e. Solvency and Leverage*

Maintaining a high level of creditworthiness as well as financial performance is vital for LLCs to access financing, negotiate favourable terms and ensure long-term sustainability. It involves effective financial management, sound business practices, timely and accurate financial reporting and proactive planning and budgeting in order to be ready to correctly address potential challenges and issues. It is important to regularly monitor the creditworthiness and financial performance of the LLC to identify issues on a timely basis. This helps to identify the areas that need improvement and enables informed decisions to support the growth and stability of the company (Normamatovich et al., 2020).

It's important to recognize that the influence and importance of these factors can significantly differ based on the certain circumstances of each LLC and the current market conditions as well as different industries. Effectively evaluating and coping with these factors is vital for enhancing the cost of capital and fostering the financial health and expansion of the LLC.

1.6. Summary of findings

To sum up, the following conclusions was made regarding the developed models:

- Capital Assets Pricing Model (CAPM) is mostly used and is based on the assumption that the cost of capital depends on the rates which are the most popular in the market, as well as on the risk connected with investments in the company.
- Gordon model is one of the types of the dividend discount model. The dividend discount model and the Gordon model are based on the next simplifications: market capitalization rates are equal at any time which means the investors always value the risk connected with a given stock in the same way; the stream of cash payments is an infinite stream of dividends; the growth rate of annual dividend payments are constant and the firm always pays dividends.
- Another broadly famous model is the Arbitrage Pricing Theory (APT). This model is known because it is claimed to be more realistic than CAPM because of its reduced prerequisites. It operates on the assumption that each investor tries to enhance its portfolio's returns while also tries to reduce or at least not increasing the risk. Investors use the arbitrage pricing theory principles to earn on different prices for identical assets to secure risk-free earning. This involves the next procedure: selling a certain security at a higher price and buying it at a lower price. Advantages of this model lies in its multifaceted nature, allowing for the evaluation of various factors influencing stock prices. But, its practical application is not as easy and have limitations and also researchers have different opinions regarding the factors determining this model.
- To determine the cost of capital of the company as a whole, the weighted average cost of capital (WACC) is used. The weighted average cost of capital is the "price" for the use of capital, the discount rate or time value of money used to convert future cash flows to their present value for all "providers of capital". The WACC indicator characterizes the level of expenses of the enterprise for the opportunity to use financial resources on a long-term basis. The WACC value varies by industry, so there is no standard value for this value. However, when considering the WACC indicator, its decline will be considered a positive trend.
- The Fama and French three-factor model was proposed in 1993 as an extension of the Capital Asset Pricing Model (CAPM) and a solution to its low predictive power problem. The model showed that future returns are related to additional factors: the size of the company and its intrinsic value.
- The EHV model focuses on country credit ratings, which, according to the authors, are decisive in the formation of the required return in developing countries. The authors (K. Erb, R. Harvey and T. Viskant) propose to evaluate the marginal required return (lower limit) of

investors in emerging markets by regression dependence relative to the constructed credit rating of the country. This is especially true for countries with a weak stock market that does not allow the use of models within the framework of the CAPM. EHV model allows in some cases to estimate the required return on equity, but does not take into account the psychological factors of risk perception. An alternative is the DCAPM model.

- The cost of capital of limited liability companies (LLCs) are influenced by some key factors like risk tolerance and return expectation of an investor, total structure of capital and also the creditworthiness of the company its financial performance market conditions industry and market and especially industry risks, scale of the company and the potential future growth, regulatory environment of industry and in the end market understanding of an investor and investors preferences
- The expected risk of an investor also influence the cost of capital. Some special industries with higher risk levels may demand greater returns, hence resulting in increased cost of capital. Additionally, the LLC's capital structure which is a balance between debt and equity financing affects the cost of capital. Increased debt levels can increase the risk and borrowing expenses for the LLC.
- The creditworthiness and financial performance of the LLC are vital elements as well and influence the cost of capital. Strong financial health and good credit ratings from rating agencies like S&P, Moody's and Fitch can lead to decreased borrowing expenses and a decreased cost of capital. Moreover, interest rates and capital accessibility can strongly affect the cost of capital as well. Economic stability of the country and lower interest rates typically means reduced cost of capital.
- Both industry and market risks are significant considerations because industries where the higher volatility is a normal situation or regulatory issues increases the risks and consequently it will increase the cost of capital. The size and growth potential of the LLC also impact the cost of capital. Smaller and newly established LLCs most probably may face higher borrowing costs because of higher risks, while larger and more growth-oriented LLCs may have access to lower-cost capital because of lower risks.
- The legal and regulatory environment also affects the cost of capital. Strong regulations and compliance requirements usually increases operating costs and affect the cost of capital. Market perception and investor confidence also play a role.

CHAPTER 2. RESEARCH METHODOLOGY

2.1 Research design

There are certain methods and procedures for finding and checking the cost of capital and its determinants in limited liability companies establish a clear framework to address the research query.

The research design of the analysis of limited liability companies' cost of capital and its influencing factors shows the overall plan and strategy for conducting the study. It involves decisions regarding the research question, data collection methods, sample selection, data analysis techniques and the overall structure of the research (Sileyew, 2019). The key components of the research design for this analysis are the following:

Research Objectives - The targets of the study such as examining the determinants of the cost of capital for limited liability companies and identifying the factors that influence their capital structure decisions are clearly defined. The objectives provide a clear vision for the research and ensure that appropriate research methods were chosen.

Research Approach - This research will use a mix of both quantitative and qualitative research methods in order to collect the numerical data and qualitative research to obtain surveys.

Data Collection Methods – Appropriate data selection and collection techniques is based on obtaining appropriate information. This involves extracting the financial data from the financial statements of certain company as well as conducting surveys among limited liability companies and also using secondary data sources and finally conducting special expert interviews. These methods are aimed to answer to the research question and ensure the receiving the dependable and credible data.

Sample Selection - The criteria for selecting the sample of limited liability companies to be included in the analysis is defined. Factors such as industry representation, size of the companies and availability of financial data are considered. The sample will show us the target population and also will provide sufficient variability in population to identify different cost of capital determinants.

Data Analysis Techniques – The techniques for data analysis that are used to analyse the gathered data are determined. This will involves special statistical analysis methods to identify the factors that can significantly influence the cost of capital. Additionally, financial ratios and other quantitative measures will be used to assess the capital structure decisions.

Ethical Considerations - Ethical considerations like data confidentiality and informed consent are also taken into consideration. It is ensured that the research adheres to ethical

guidelines and protects the rights and privacy of the participants involved and their confidentiality.

Timeline and Resources – For data collection, analysis and report writing the timeline was created and also used in the research. For data analysis and access to financial databases were identified and found.

Limitations and Delimitations - The limitations and delimitations of the research design are acknowledged. This includes recognizing any constraints in terms of data availability, sample size or the generalizability of the findings.

The research methods are designed in order to receive the accuracy in the analysis of limited liability companies' cost of capital and its influencing factors. The research design is transparent and also aligned with the research objectives to ensure that findings are reliable and also valid.

2.2. Research methods

Methods of research are the special methods, strategies and processes utilized to collect and evaluate data with the aim of responding to research inquiries or examining hypotheses.

Quantitative research includes methodically collecting and analysing numerical data in an impartial manner. The objective is to find out statistical conclusions about a population through the data. This approach emphasizes measuring and quantifying variables, exploring relationships between them and testing hypotheses (Bloomfield & Fisher, 2019). The study involves the following methodologies affiliated with quantitative research:

- Data Collection method is used in the study. This method involves the collection of numerical data through techniques such as surveys, experiments and existing datasets. Surveys often use close-ended questions and standardized scales to elicit responses that can be quantified. Survey with 5 point Likert scale is used in the research work.

- In the thesis, the concept of Sample Size also was used: Quantitative research generally necessitates sizable sample sizes to ensure statistical distinction and representativeness of the intended population. Sampling methods like (for example random sampling or stratified sampling) are frequently utilized.

- Statistical Analysis was utilized in the thesis: Quantitative data is analysed using statistical methods to identify patterns, trends and relationships. Descriptive statistics summarize the data, while inferential statistics are used to draw conclusions and make statistical inferences.

- Graphical analysis is used in the study: Quantitative research typically presents findings in numerical form, such as tables, charts, or graphs.

Quantitative research provides a systematic and rigorous approach to studying phenomena, establishing relationships between variables and making evidence-based conclusions. It is widely used in fields such as psychology, sociology, economics and market research, among others.

Qualitative research is one of the methods for finding out that centers around comprehending and deciphering social phenomena by exploring and breaking down non-numerical information in-depth. The objective is to reveal rich and nuanced perceptions, implications and encounters from the standpoint of individuals or groups involved. Qualitative methods, like analysis are used as well. Surveys are used both in quantitative and qualitative aspect.

2.4. Survey

In this study, as one of the methods of primary data collection, an online questionnaire is used to find out views and opinions of the employees of finance, accounting, audit and executive board members on factors affecting cost of capital of LLCs. The development of the Internet makes it easier and faster to collect answers, so the questionnaire was created on the Google form platform. This platform was built on the basis of the convenience of the interface, an easy way to distribute, as well as the ability to immediately save the results in Excel format. The questionnaire for this study required the respondents to answer the questions expressing their opinions towards factors affecting cost of capital in LLCs.

The first part of questionnaire requires the participants to fill demographic information: age, gender, occupation. This part consists of 9 questions. It also focuses on measuring the perception of respondents about cost of capital and LLC. It helps to understand in what content the respondents are aware about cost of capital in LLCs. The second part of survey is about factors influencing cost of capital in LLCs. This part contains 22 questions.

Table 4.

The survey structure (Source: developed by author)

| № | Section | Explanation |
|----------|--|--|
| 1-4 | Demographic | All data relevant to demographic information is collected, such as gender, age, education, occupation. |
| 5-9 | Awareness about LLC and cost of capital of LLC | Helpful Data to understand the general awareness of respondents about LLC and cost of capital |
| 1-22 | Factors influencing cost of capital | This section is the main one. Collected data helps to |

| | | |
|--|--|--|
| | | analyze the factors affecting cost of capital in LLC |
|--|--|--|

The link to the survey was sent to the management team of the most leading LLCs in Azerbaijan and they were asked to support in the conduction of survey by distributing the link amongst finance and accounting teams as well as managerial team. The link also was sent to several LLC auditing teams for support in the matter as well.

Sampling strategy - Since the study does not have a specific narrowly targeted sample of participants, non-probability sampling methods were used, since this method is used with limited capabilities of the researcher. These methods include the convenience sampling method and the snowball sampling method. The first method was chosen because of its easy access to survey participants. The link to the survey will be left in groups on social networks with a large number of students and graduates of economics, management and finance faculties.

Sampling size will be used by means of online platforms to identify the number of participants that are required to participate in the survey in order to get accurate results.

Sampling size is calculated by using the online calculation site Select Statistical Services (Figure 1).

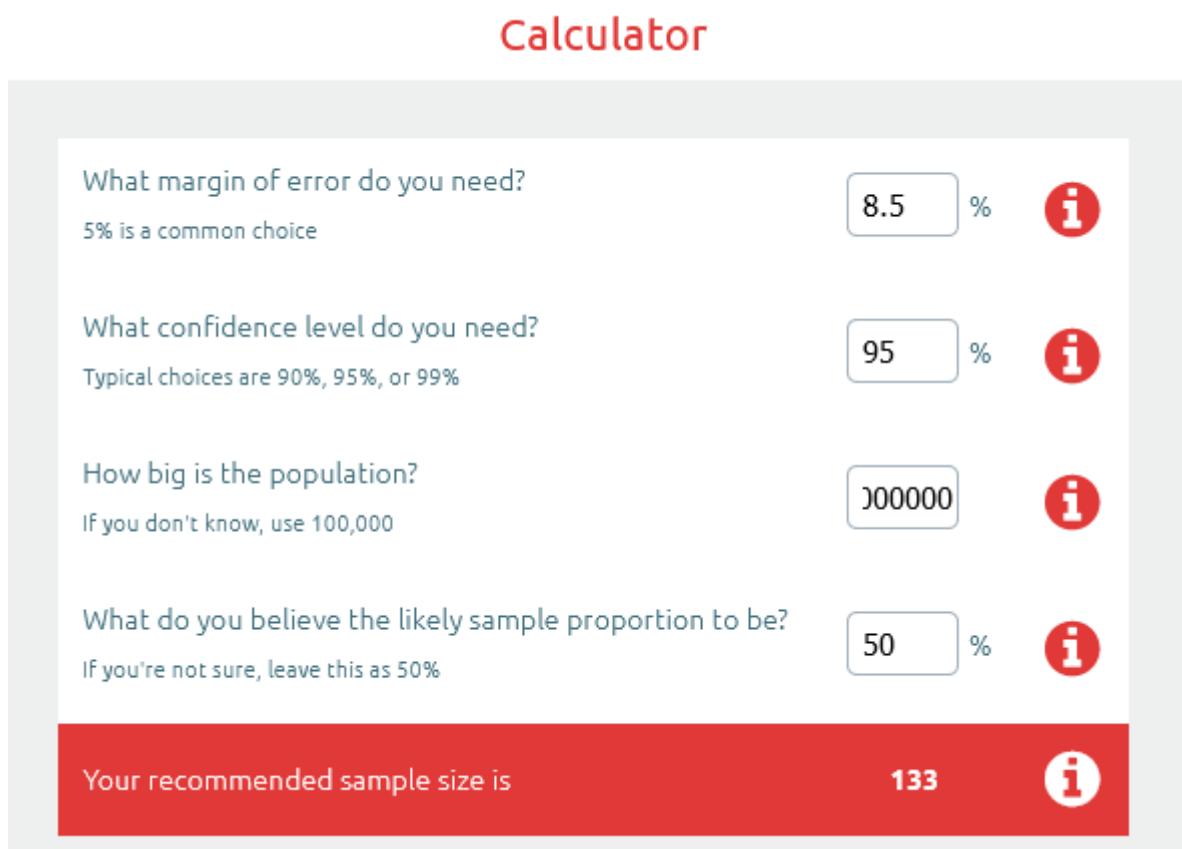


Figure 1. Sample size calculation (Source: Select Statistical Services)

As it can be seen from the calculation, minimum 133 respondents are required to participate in the survey in order to get accurate results.

Data processing methods: The analysed stage of the information obtained is an important stage in any research. The main result will depend on the chosen method. By choosing the wrong or inappropriate method, the result may not be appropriate for the task. Therefore, the goal and objective must be first defined and then the desired method should be selected.

The aim of the study is to determine the factors influencing to the cost of capital. The goal will be achieved by using research questions. To conduct the research and provide the final result, it is necessary to use the methods of statistical analysis. After a sufficient number of participants answered the questionnaire, the results will be given in the thesis and the responses will be analysed.

2.5. Brief info about “GRANDMART” LLC – supermarkets chains

Grandmart supermarket chain, which has been operating in the retail market of Azerbaijan for almost 20 years, is currently at the disposal of customers with more than 30 branches. Grandmart supermarket chain, which started operating with its first branch in the capital city of Baku, has also opened branches in other regions of the country. It should be noted that the supermarket chain sells more than 40,000 products. About 1,500 employees are currently working in the Grandmart Supermarket Network. The central warehouse located in the capital city of Baku on an area of 5000 square meters is equipped with cooling-heating systems and trucks. Grandmart supermarket, which opened in Aktau, Kazakhstan on April 9, 2021, is known as the first retail brand operating outside the country's borders. The Aktau branch located on an area of 3000 square meters is also the largest supermarket in the city.

According to the report by AZERTAC – Official News Agency of Azerbaijan, the total volume of sales of "GrandMart" in 2021 was \$78,281,922. This is 21% more than the previous year, so in 2020 the turnover of "GrandMart" was \$64,695,803.

The cost of sales in 2021 was \$64,021,746. This is 23% more than in 2020. In 2020, the cost of sales was \$52,050,200.

In 2021, the company's other income amounted to \$5,392,134 - which is almost twice as much as in 2020, the previous year other income was \$2,751,088.

In 2022, the company's sales revenue, that is, the annual sales turnover, was \$119,518,837. Compared to 2021, the sales turnover increased by \$41,236,915.

As a result, the company's total profit from sales in 2022 was \$3,406,594.

The cost of capital of the company was 10.5% (according to AzerTac) the market value is \$58,823,529, the volume of sales is \$119,518,837.

CHAPTER 3. DATA ANALYSIS

3.1 Industry analysis of Grandmart's of Limited Liability Company

Understanding the grocery industry means knowing our strengths, weaknesses, opportunities and threats (SWOT) and how competition, suppliers, buyers, substitutes and new players shape things (Five Forces). It's like a map guiding us—strong distribution is great, but tough competition is a challenge. Online shopping and healthy trends offer opportunities, but supply problems or regulations are threats. Knowing these helps make smarter moves in this competitive environment.

Strengths

- Steady Demand - people always need food, ensuring a steady stream of customers.
- Variety of Product - they offer lots of different foods to suit different tastes.
- Good Distribution - they have efficient ways to get products to stores.
- Brand Loyalty - many customers stick to their favorite brands.

Weaknesses

Thin Profits - grocery stores don't make a lot per item sold.

Lots of Competition - many stores fight for customers.

Seasonal Sales - some products sell less at certain times.

Supply Issues - sometimes they run out of products.

Quality Control Challenges - it's hard to keep all products consistently good.

Opportunities

Online Growth - more people buy groceries online.

Health Focus - healthy food is popular and in demand.

Sustainability - people want products that are eco-friendly.

Global Markets - chance to sell in new countries.

Threats

New Competitors - tech companies and others are entering the grocery market.

Price Wars - competing on price can hurt profits.

Changing Preferences - people might start wanting different kinds of food.

Rules Change - laws about food safety might change.

Supply Disruptions - problems in getting products can happen due to many reasons.

During the research Michael Porter's five model also was applied. Forces model to analyze this sector. This model helped dissect the competitive landscape by exploring factors like new entrants, buyer power, supplier influence, substitutes and competitive rivalry.

New Competitors Threat - Starting a grocery store is not expensive, but large grocery stores like (Bravo, Araz, Neptun) are already in the market and make it tough for new companies. Online grocery services usually offer a new way in.

Supplier Bargaining Power - Suppliers for food items have some power, but grocery chains push for better deals.

Buyer Bargaining Power - Shoppers hold the cards here. With many options, they can easily switch between stores, forcing competitive prices and services.

Substitute Threat - There are a few alternatives, but regular grocery stores are where most people go for their food needs.

Competition Level - It's a tough fight among supermarkets, convenience stores, discount shops and online sellers. Standing out with different products, prices and services is important.

3.2 Analysis of Limited Liability Company "GrandMart" cost of capital

Based on the provided financial information for "GrandMart," we can conduct an analysis of the company's cost of capital.

Table 5: Balance sheet as at December 31, 2022

| Item | Amount in USD |
|-----------------------------------|----------------------|
| Property, plant and equipment | 9,978,899 |
| Intangible assets | 938,355 |
| Deferred tax assets | 183,280 |
| Receivables from shareholders | 349,279 |
| Prepayment for non-current assets | 316,515 |
| Right-of-use assets | 16,507,705 |
| Total non-current assets | 28,274,032 |
| Inventories | 16,654,995 |
| Cash and cash equivalents | 2,197,796 |
| Trade and other receivables | 568,821 |
| Receivables from related entities | 2,798,354 |
| Receivables from shareholders | 1,835,724 |
| Other assets | 2,532,263 |
| Total current assets | 26,587,952 |
| Total assets | 54,861,985 |

| | |
|--|-------------------|
| Share capital | 7,070,412 |
| Subscription receivables from shareholders | (2,985,882) |
| Retained earnings | 1,690,235 |
| Total equity | 5,774,765 |
| Borrowings | 2,382,752 |
| Borrowing on behalf of shareholder | 3,237,108 |
| Lease liabilities | 12,780,602 |
| Total non-current liabilities | 18,400,461 |
| Borrowings | 771,512 |
| Borrowing on behalf of shareholder | 1,835,724 |
| Tax provision | 662,194 |
| Advance received | 17,039 |
| Provision | 275,081 |
| Lease liabilities | 2,725,697 |
| Trade and other payables | 17,457,678 |
| Payable to related entities | 6,249,476 |
| Other liabilities | 692,359 |
| Total Liabilities | 49,087,220 |
| Total Liabilities and Equity | 54,861,985 |

Source: internal data from GrandMart LLC

GrandMart's profit before tax is \$3,765,365. This figure is important in determining the overall financial health of the company and its ability to generate returns for investors. GrandMart's profit before tax is \$3,765,365 and the profit for the year is \$3,406,594. This indicates positive profitability.

The company has significant non-cash adjustments, including depreciation of PPE, depreciation of ROU assets and amortization of intangible assets. These adjustments impact the reported profit and should be considered in cost of capital calculations.

The operating cash flow before changes in working capital is \$9,397,031. This represents the cash generated by GrandMart's core business operations before accounting for changes in working capital.

- Operating cash flow before changes in working capital: \$9,397,031.
- Net cash flow from operating activities: \$8,809,524.
- Net cash outflow from investing activities: \$4,870,108.
- Net cash outflow from financing activities: \$3,452,352

- Net increase in cash and cash equivalents: \$486,386.

GrandMart experienced various changes in working capital, including receivables, inventories and payables. Managing these components efficiently is essential for optimizing working capital and subsequently, the cost of capital.

Changes in Working Capital:

- Notable changes in trade receivables, inventories and payables.
- Effective working capital management is important for liquidity and minimizing financing costs.

Cash Generated from Operating Activities:

- Cash generated from operating activities before interest and tax is \$11,031,461.

Total Assets and Equity:

- Total non-current assets: \$28,274,032
- Total current assets: \$26,587,952.
- Total equity: \$5,774,765

Total Liabilities:

- Total non-current liabilities: \$18,400,461.
- Total current liabilities: \$30,686,759

Profitability Ratios:

$$\text{Gross Profit Margin} = (\text{Gross Profit} / \text{Revenue}) \times 100$$

$$\text{Gross Profit Margin} = (24,108,291 / 119,518,837) \times 100$$

$$\text{Gross Profit Margin} \approx 20.17\%$$

$$\text{Operating Profit Margin} = (\text{Operating Profit} / \text{Revenue}) \times 100$$

$$\text{Operating Profit Margin} = (5,295,518 / 119,518,837) \times 100$$

$$\text{Operating Profit Margin} \approx 4.43\%$$

$$\text{Net Profit Margin} = (\text{Net Profit} / \text{Revenue}) \times 100$$

$$\text{Net Profit Margin} = (3,406,594 / 119,518,837) \times 100$$

$$\text{Net Profit Margin} \approx 2.85\%$$

Liquidity Ratios

$$\text{Current Ratio} = \text{Current Assets} / \text{Current Liabilities}$$

$$\text{Current Ratio} = 26,587,952 / 30,686,759$$

$$\text{Current Ratio} \approx 0.87$$

$$\text{Quick Ratio} = (\text{Current Assets} - \text{Inventories}) / \text{Current liabilities}$$

$$\text{Quick Ratio} = 9,932,957 / 30,686,759$$

Quick Ratio ≈ 0.32

These ratios provide insights into GrandMart's profitability and liquidity. The gross profit margin indicates the efficiency of production, while operating and net profit margins show the company's ability to manage operating expenses. Current and quick ratios assess the company's liquidity and ability to cover short-term liabilities. Interpretation of these ratios should consider industry benchmarks and historical trends for a more comprehensive analysis.

The net cash flow from operating activities is \$8,809,524., indicating the cash generated or used by the company's day-to-day operations.

GrandMart had significant cash outflows from investing and financing activities, totalling \$4,870,108 and \$3,452,352 respectively. These activities include capital expenditures, acquisitions, debt repayments and other financing transactions.

The net increase in cash and cash equivalents for the year is \$486,386 contributing to the ending cash balance.

Factors influencing the cost of capital include the interest paid, income tax paid and any extraordinary gains or losses. Additionally, economic conditions, market risks and the company's risk profile will impact the cost of both debt and equity.

Assessing the cash and cash equivalents position at the end of the year (\$2,197,796) provides insights into GrandMart's liquidity, which is essential for short-term obligations.

Additionally, the Altman Z-Score was utilized to assess the financial well-being of Grandmart

$$Z=1.2A+1.4B+3.3C+0.6D+1.0E$$

A=Working Capital/Total assets

B=Retained Earnings/Total Assets

C=EBIT/Total Assets

D=Market Value of equity/Total Liabilities

E=Total sales/Total Assets

$$Z=1.2*(-0.074)+1.4*0.03+3.3*0.097+0.6*0.12+1*3.73$$

Altman Z score is equal to 4 and it can be considered as a financially stable company with very low risk of bankruptcy.

Table 6: WACC calculation of GrandMart

| WACC calculation of Grandmart | | | |
|-------------------------------|-----------|---------------|--|
| Component | Damodaran | Duff & Phelps | Comment |
| Risk-free rate | 3.87% | 3.87% | Reflects the return that a US investor would expect to receive on a risk-free 20 year US Treasury Bond |
| Equity risk premium | 5.50% | 5.50% | Reflects the expected premium of US corporate large-cap equity investments over US treasuries |
| Beta (unlevered) | 0.45 | 0.70 | Reflects the relative risk of the subject company's industry as compared to the S&P 500 index, without taking into consideration the |

| | | | |
|-------------------------------------|---------------|---------------|--|
| | | | industry's average (optimal) capital structure |
| Beta (market/relevered) | 0.67 | 1.06 | Calculated based on the formula: Unlevered beta x (1 + ((1 - income tax) x (industry average Debt to total invested capital ratio))) |
| Small size risk premium | 3.02% | 3.02% | Reflects a premium/(discount) for size compared to guideline/industry companies from Mornigstar research |
| Country risk premium | 4.32% | 4.32% | Reflects risk for having the subject company's primary operations in Azerbaijan |
| Currency risk premium | 3.97% | 3.97% | Reflects a premium for risk of cash flow denominated in AZN as compared to USD cash flow |
| Specific risk premium | - | - | Reflects risk for uncertainty of holding investment in a specific firm taking into account riskiness of its forecast cash flows |
| Cost of Equity | 18.87% | 21.02% | Reflects required rate of return on equity |
| Cost of Debt (pre-tax) | 10.0% | 10.00% | Reflects the average interest rate for AZN denominated borrowed funds by companies in Azerbaijan |
| Tax rate | 20.00% | 20.00% | Corporate income tax rate according to the Tax Code of Republic of Azerbaijan |
| Cost of Debt (after-tax) | 8.00% | 8.00% | Reflects required rate of return on borrowed funds for the Company's lenders |
| Share of Equity in Invested Capital | 39.69% | 35.48% | Calculated based on the formula: (1-Share of equity in invested capital) |
| Share of Debt in Invested Capital | 60.31% | 64.52% | Reflects the Damodaran's industry average debt to invested capital ratio & Company's target figures |
| WACC | 12.31% | 12.62% | Required rate of return on equity and debt |
| Average | | 12.47% | |

Source: developed by the author

The risk-free rate is 3.87%, reflecting the return that a US investor would expect to receive on a risk-free 20-year US Treasury Bond. In this context, it's important to note that the risk-free rate used is based on US Treasury Bonds, which might not precisely reflect the risk-free rate in Azerbaijan. It is a foundational component for calculating the cost of equity. The equity risk premium is 5.50%, representing the expected premium of US corporate large-cap equity investments over US treasuries. This premium compensates investors for the additional risk associated with investing in equities rather than risk-free assets. The unlevered beta is 0.45, reflecting the relative risk of the subject company's industry as compared to the S&P 500 index without considering the company's debt. The market/relevered beta is 0.67, calculated based on the unlevered beta and the industry average debt to total invested capital ratio. This leveraged beta accounts for the impact of the company's debt on its risk profile. The small size risk premium is 3.02%, reflecting a premium/(discount) for the size of the company compared to guideline/industry companies. The country risk premium is 4.32%, indicating the additional risk for having the subject company's primary operations in Azerbaijan. This premium accounts for the country-specific risks. The currency risk premium is 3.97%, reflecting a premium for the risk of cash flow denominated in Azerbaijani Manat (AZN) as compared to USD cash flow. The cost of equity is calculated using the Capital Asset Pricing Model (CAPM) and is 18.87%. It represents the required rate of return on equity for investors. The cost of debt is 10.00%, reflecting the average interest rate for AZN-denominated borrowed funds by companies in Azerbaijan. The corporate income tax rate is 20.00%. The cost of debt after-tax is 8.00%, reflecting the required rate of return on borrowed funds for the company's lenders, considering the tax shield. The proportion of equity and debt in the company's capital structure is calculated

based on industry averages and the company's target figures. The WACC is the weighted average of the cost of equity and the after-tax cost of debt, taking into account the proportions of equity and debt in the capital structure. It is 12.31%.

The calculated WACC of 12.31% represents the average rate of return that GrandMart LLC needs to provide to its investors (both equity and debt holders) to attract and retain capital in Azerbaijan. It is used as a discount rate for evaluating potential investment projects or determining the company's overall cost of financing. The components of WACC are influenced by various factors including market conditions, country-specific risks and the company's specific financial structure in the context of operating in Azerbaijan.

3.3 Analysis of the factors influencing cost of capital of "GrandMart" LLC

To analyse the factors influencing the cost of capital for GrandMart LLC, the financial information should be considered as follows:

GrandMart generated \$11,031,461 from its operating activities before interest and taxes. This positive cash flow indicates the company's ability to generate funds from its core business operations.

GrandMart paid \$1,792,833 in interest and \$429,104 in income tax. These payments contribute to the overall cost structure and affect the company's net cash flow.

The net cash flow from operating activities is \$8,809,524 reflecting the cash generated or used by the company's operational activities after accounting for interest and taxes.

GrandMart had net cash outflows from investing activities (\$4,870,108) and financing activities (\$3,452,352). These activities include investments in assets, capital expenditures, debt repayments and other financing transactions.

The net increase in cash and cash equivalents is \$486,386. This represents the change in the company's cash position during the period.

GrandMart started the year with \$1,533,653 in cash and cash equivalents and ended with \$2,197,796. The ending cash balance is important for liquidity and short-term obligations.

Profit for the year is \$3,406,594 with revenue of \$119,518,837 cost of sales at \$95,410,545, gross profit of \$24,108,292 and operating profit of \$5,295,518. These figures contribute to the overall financial health and profitability of the company.

Total non-current assets amount to \$28,274,032 while total current assets are \$26,587,952. Total equity stands at \$5,774,765 On the liabilities side, total non-current liabilities are \$18,400,461 and total current liabilities are \$30,686,759.

Taking into account the above mentioned analysis, factors influencing Cost of Capital would be the following:

Debt Levels - the proportion of debt in the capital structure need to be evaluated. The interest paid on debt contributes to the overall cost of capital.

Equity Financing - the cost of equity, which is influenced by the company's risk profile, market conditions and investor expectations need to be considered.

Operating Performance - the company's operating profit and overall profitability impact its ability to cover interest and attract investors.

Liquidity Position - the ending cash balance and liquidity ratios influence the company's financial flexibility and cost of capital.

Investment and Financing Decisions - how the company's investment and financing decisions impact its cash flows and overall capital structure need to be assessed.

Market Conditions - external factors such as interest rates, economic conditions and industry trends that may affect the cost of capital need to be taken into account.

The mix of debt and equity in GrandMart's capital structure is a critical factor. The proportion of each component influences the overall cost of capital. A higher level of debt may result in lower overall costs, but it increases financial risk.

The interest rate on debt, symbolizing the expense of borrowed capital, holds considerable weight. This rate is subject to fluctuations driven by prevailing market interest rates, the company's credit standing and any particular terms linked with the debt.

On the other hand, the cost of equity is shaped by how investors view the company's risk profile. Elements like the company's beta, market dynamics and the risk-free rate contribute to this assessment. When investors perceive elevated risk, it often leads to a higher cost of equity.

General economic conditions, interest rates and the overall state of the financial markets impact the cost of capital. Changes in these conditions may affect the company's ability to raise funds and the associated costs.

The industry in which GrandMart operates and its specific business risks contribute to the cost of capital. Industries with higher inherent risks may face higher costs of capital.

GrandMart's risk profile, including its operational efficiency, historical performance and growth prospects, influences the cost of capital. Stable and well-established companies may have a lower cost of capital compared to those with higher uncertainties.

3.4 Survey Results

The survey link was sent to the local LLC companies' executive board, finance and accounting teams and audit companies. The required number of participants according to sampling was 133. The required number – 133 responses were obtained. The survey questionnaires can be found in the Appendix 1.

First, the demographic part of the questionnaire is provided as follows:

1. What age category do you fall under?

133 responses

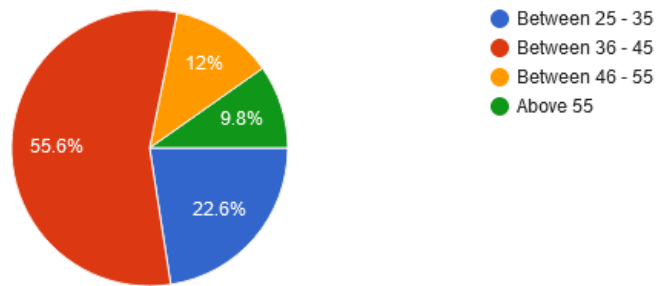


Figure 2: Age category of the respondents.

As it can be seen from the Figure 2, the vast majority of the respondents (55,6%) are under the age of 36 – 45 years old).

2. What speciality category do you fall under?

133 responses

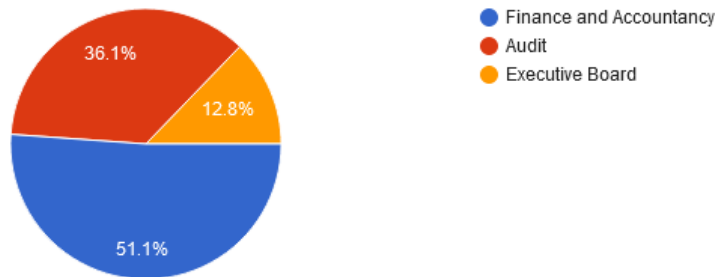


Figure 3: Speciality category of the respondents

The most percentage of respondents (51,1%) are in finance and accountancy, 36,1% are in audit team and 12,8% are in executive board.

3. In which region of Azerbaijan do you currently reside?

133 responses

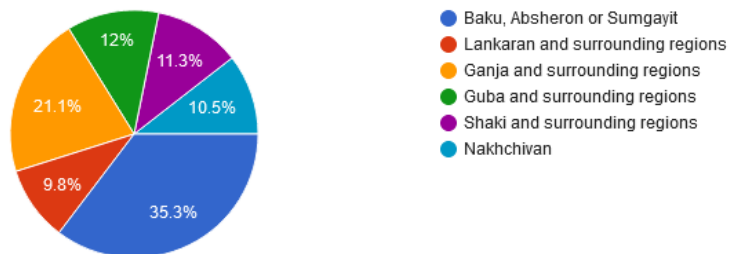


Figure 4: The region of the respondents within Azerbaijan

The most percentage of the respondents (35,3%) are from Baku, Absheron or Sumgayit; 21,1% are from Ganja, 12% are from Guba, 11,3% are from Shaki, 10,5% are from Nakhchivan and 9,8% are from Lankaran.

4. What education category do you fall under?

133 responses

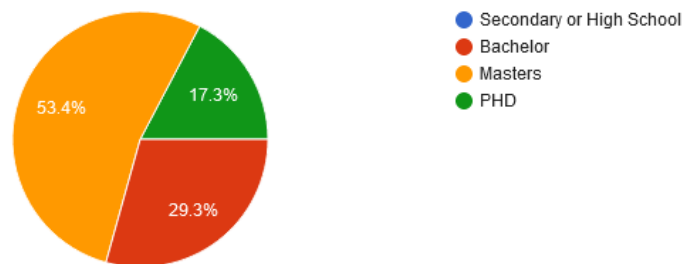


Figure 5: Education category of respondents

53,4% of respondents are master's degree holders, 29,3% are bachelor degree holders and 17,3% are PHD degree holders.

The next questions show how familiar are the respondents with the term LLC and their knowledge and awareness about LLC and cost of capital in general.

5. How familiar are you with the term "Limited Liability Company" (LLC)?

133 responses

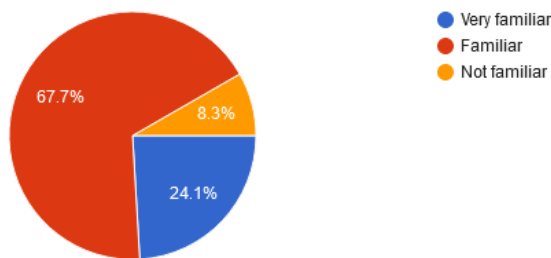


Figure 6: Familiarity of the respondents with the term LLC (Limited Liability Company)

67,7% of the respondents are familiar with the term LLC very well, 24,1% of respondents stated that they are familiar with the term LLC and 8,3% stated that they are not familiar.

Most respondents from the finance team, audit team and executive board of LLCs are very familiar with the term "Limited Liability Company" (LLC). This is important, as a strong awareness of the business structure is essential for effective financial management and decision-making.

6. Can you briefly describe the primary purpose or advantages of forming a Limited Liability Company (LLC)?



133 responses

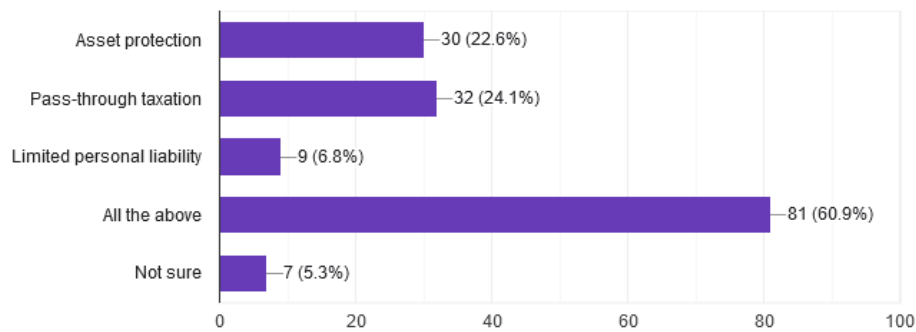


Figure 7: Primary purpose or advantages of forming LLC

The question in Figure 7 is multiple choice question, one person can choose more than one answer. 22,6% (30 respondents) answered that asset protection is the primary purpose for forming LLC, 24,1% (32 respondents) answered pass-through taxation, 6,8% (9 respondents) answered limited personal liability, 60,9% (80 respondents) answered all the above mentioned purposes or advantages and 5,3% (7 respondents) answered that they were not sure.

Respondents can identify the primary purposes or advantages of forming an LLC, such as asset protection, pass-through taxation and limited personal liability. These responses indicate a sound understanding of the benefits associated with this business structure.

7. Are you aware of the steps involved in forming an LLC?

133 responses

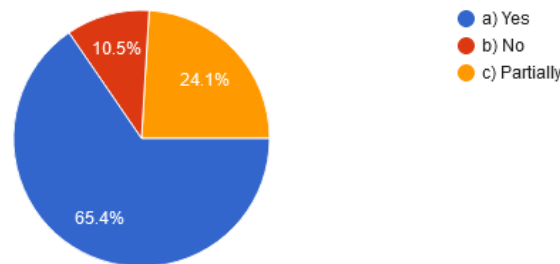


Figure 8: Awareness about the steps involved in forming LLC

65,4% answered that they are aware about steps involved in forming LLC, 24,1% responded stating that they were partially aware and 10,5% responded that they were not aware.

The majority of respondents are aware of the steps involved in forming an LLC. This knowledge is vital, especially for those in finance and executive roles, as they may be involved in the decision-making process related to the company's legal structure.

8. How would you define the concept of "cost of capital" as it relates to business finance?



133 responses

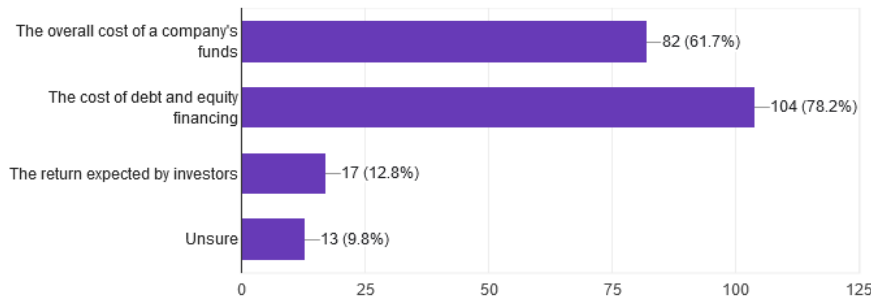


Figure 9: The concept of “cost of capital”

The question in Figure 9 is multiple choice question, one person can choose more than one answer. 61,7% of respondents replied saying the overall cost of a company’s funds, 78,2% replied saying the cost of debt and equity financing, 12,8% responded saying the return expected by investors and 9,8% answered saying “unsure”.

Respondents can define the concept of "cost of capital" as the overall cost of a company's funds and the cost of debt and equity financing. This level of understanding is important for financial decision-making, including investment choices and capital structure management.

9. In your opinion, why is understanding the cost of capital important for individuals or businesses operating as Limited Liability Companies?



133 responses

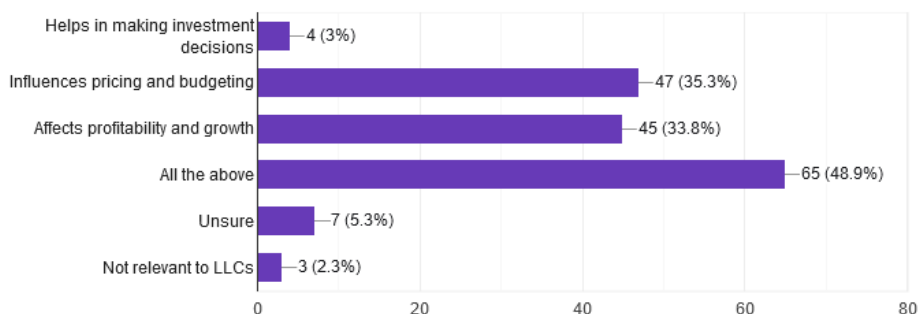


Figure 10: The importance of cost of capital understanding for LLCs

The question in Figure 10 is multiple choice question, one person can choose more than one answer. In chart 10 we can observe that only 3% of respondents replied that cost of capital understanding helped in making investment decisions, while 35,3% of respondents said that this kind of understanding affected their opinion on pricing and preparing budget, 33,8% of respondents said this understanding affected profitability and growth, 48,9% of respondents answered saying everything that was mentioned was important, 5,3% said they were unsure and 2,3% responded it was not relevant to LLCs.

The responses, including understanding the impact on investment decisions, pricing, budgeting, profitability and growth, shows us a comprehensive awareness of the significance of

the cost of capital for LLCs. This indicates a strategic understanding of financial management within the context of the specific business structure.

The next questions are related to the factors influencing the cost of capital in LLCs.

1. How do you perceive the influence of business structure on the cost of capital for LLCs? [Copy](#)

133 responses

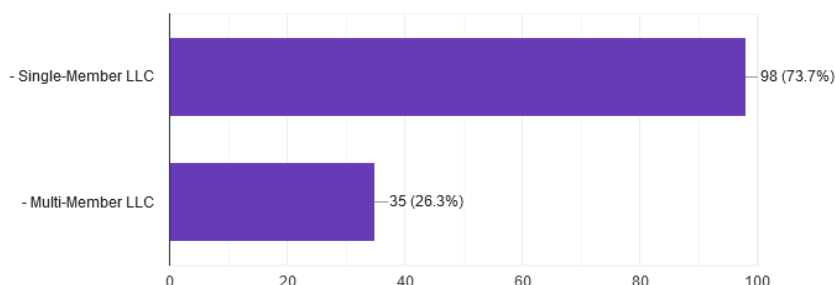


Figure 11: Influence of business structure on the cost of capital for LLCs

The question in Figure 11 is multiple choice question, one person can choose more than one answer. From the perspective of Figure 11, we see that nearly three-fourths (73.7 %) prefer single-member LLCs. The decision may come as a result of simplicity of management, ease in making decisions and ownership structure. Respondents may also value the single-member LLC's potent combination of self-control over decision making and operations, which can result in more rapid and decisive action. Moreover single-member LLCs are usually taxed as pass through entities which may be advantageous and simpler to report.

The 26.3% of those who responded in favor of multi-member LLCs hope for more emphasis on collaboration, sharing a variety of skills and distributing responsibilities within the company structure. Having multiple people in the same LLC will provide respondents with the benefits of shared decision-making and working together. Multi-member LLCs can provide risk mitigation through the diversification of skills, expertise and financial contributions.

The decision on whether to have a single-member or multi-member LLC can affect the cost of capital. The business structure of the single-member LLC is simple and it may be difficult to find various sources of funding. Multi-member LLCs, with shared responsibilities, have a somewhat more complicated structure but the potential advantage of pooled resources. They may select their type of LLC from strategic considerations such as the industry they are in, growth plans and requirements for outside investors. The preference for single or multi-member LLCs can be influenced by the specific goals and characteristics of the business. In terms of the selection of an LLC form, this can also be related to legal and regulatory issues. Understanding the legal implications and compliance requirements is important for mitigating risks and ensuring the efficient functioning of the business.

2. In your opinion, what are the key risk factors that commonly impact the cost of capital for LLCs?



133 responses

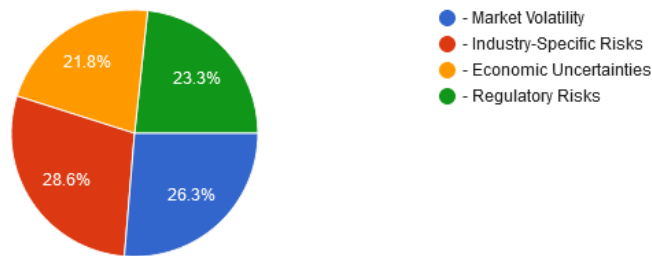


Figure 12: Key risk factors affecting the cost of capital for LLCs

Moreover, 26.3% of respondents indicate that the main factor affecting the cost of capital for an LLC is market volatility. Financing is also influenced by market uncertainties, including interest rates, confidence among investors and the overall stability of the economy. Respondents probably are worried about the impact that unpredictable market conditions will have on their costs of capital.


A slightly higher percentage of respondents (28.6%) consider industry-related risks as a significant factor which affect the cost of capital. Financing decisions will inevitably be influenced by a variety of risks related to industry. Examples include changes in technology, regulation or even competition. Respondents be sensitive to the challenges and uncertainties that exist within their own industries.

21.8% of respondents cite economic uncertainties as the major risk factor - but this is low by comparison with other factors. Global economic uncertainty due to factors such as inflation, recession or global economic conditions may become more difficult to foresee cash flows and financing requirements in the future. The impact of the overall economic environment on their cost of capital may worry respondents.

The 23.3% of respondents see regulatory risks as a serious danger to the cost of capital. After all, regulatory risks (including changes in the law and compliance requirements) can create uncertainty about financial planning. Respondents probably are attentive on how changes in the regulatory environment can influence the cost of capital.

Taken together, the answers affirm a very high degree of risk consciousness among respondents. This is awareness that costs of capital for LLCs can be heavily influenced by factors beyond their own control. The fact that respondents identified multiple risk factors suggests a nuanced understanding of the multifaceted challenges that can impact financing decisions. Businesses may need to develop strong and reliable risk mitigation strategies to address the identified factors. This could involve scenario planning, diversification and staying informed about industry and regulatory developments. The ability to adapt to changing market

conditions, industry trends and regulatory landscapes is important for mitigating the impact of identified risk factors on the cost of capital. Given the dynamic nature of these risk factors, ongoing monitoring and adaptability will be essential for LLCs to make informed financing decisions. Strategies for managing market volatility, industry-specific risks, economic uncertainties and regulatory risks may need to be tailored to the specific context of each LLC.

3. How do LLCs typically manage their debt obligations, and what impact does this have on the cost of capital? 
133 responses

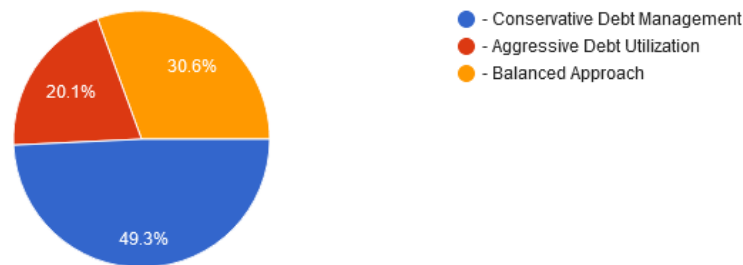


Figure 13: Management of debt obligations by LLCs and impact on the cost of capital

Most respondents would prefer conservative debt management (49.3%). It is certainly likely that the respondents who tend toward conservative debt management do so in order to achieve a sense of stability and risk minimization. This approach usually provide an opportunity to limit debt levels and focusing on maintaining a strong financial position. Another sizable group of respondents (20.1%) support aggressive use of debt. Respondents opting for aggressive debt utilization may be seeking to leverage debt strategically to fund growth opportunities. This approach typically involves taking on higher levels of debt to potentially amplify returns. About one-third (30.6%) of the respondents opted for a balanced approach to managing debt. Respondents choosing a balanced approach are probably looking for a middle ground, combining both the benefits of conservative practices and the strategic use of debt in order to grow. This approach aims to optimize the cost of capital while managing associated risks.

These answers indicate that these people are concerned with the debt risk-return relationship. The principle of the conservative approach is risk minimization while on the other hand, the aggressive approach is greater return provides also increased risk. The distribution of responses may show us that businesses are strategically evaluating their approach to debt management and also precisely try to considering both short-term and long-term financial goals. Respondents favouring conservative debt management are prioritizing financial stability, emphasizing the importance of maintaining a solid financial foundation while respondents that advocating for aggressive debt utilization may be focused on utilizing debt as a strategic tool for expansion and growth. The large group that say balanced approach is needed tells us that there is

an understanding of how to balance the risk and return in use of debt. When the overall economic environment changes, the popularity of various debt management techniques will likewise change. Changes in interest rates can impact the cost of debt, influencing the attractiveness of various debt management strategies. Industry-related considerations may play a role in determining the optimal debt management approach, with certain sectors favouring specific strategies. Businesses may need to adapt their debt management strategies and be flexible based on changing market conditions, industry dynamics and overall economic outlook. Regular monitoring and assessing of debt-related metrics and financial health will be important for making informed decisions and adjusting strategies as needed.

4. To what extent do interest rates commonly affect the cost of capital for LLCs?

133 responses

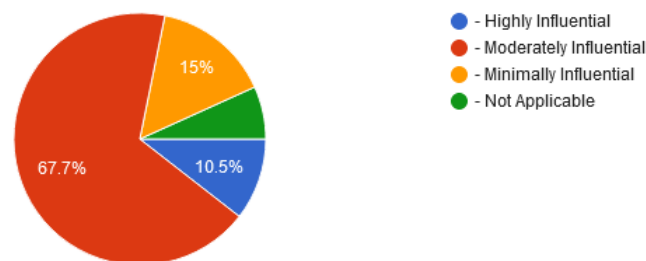


Figure 14: Interest rates impact on cost of capital for LLCs

The majority of respondents (67.7%) consider interest rates to be moderately influential on the cost of capital for LLCs, hence, it reflects that a majority of respondents feels the changes in interest rates have an important effect on the cost of capital. But they likely don't see interest rates as being the only deciding factor. A sizable percentage of respondents (15%) consider interest rates to have a small influence on the cost of capital. Those in this group may feel that interest rates only have a small influence on the cost of capital other factors, like market conditions, industry dynamics as well as company-specific considerations, are more important and influence more on the financing decisions. A relatively small percentage of respondents (10.5%) admit that interest rates extremely important in determining the cost of capital. This subset of respondents probably considers changes in interest rates to be a critical factor in determining their cost of capital. They may closely monitor interest rate movements and make strategic financial decisions based on these changes. A minority of respondents (6.8%) indicated that interest rates are not applicable to the cost of capital for their LLCs. Perhaps this group has its own special business environment, or perhaps a different industry that sets interest rates or they might have particular forms of financing that are less sensitive to interest rates.

The spread of responses reflects the diversity of factors affecting cost of capital. Interest rates are important, but respondents also take into account a number of other factors in their choices of how to finance. The majority of respondents recognizing a moderate influence

suggest that LLCs are probably engaging in adaptive financial planning, considering interest rates among various factors that impact the cost of capital. Among many factors affecting cost of capital, interest rate is only one indicator.

The diversity in responses indicates that businesses may have varying degrees of sensitivity to interest rate changes based on their industry, market position and financial structures. Respondents may need to maintain dynamic financial strategies, adjusting their approach to interest rate risk based on evolving economic and market conditions.

5. Are there common trends in equity issuance among LLCs, and how does this impact the cost of capital?

133 responses

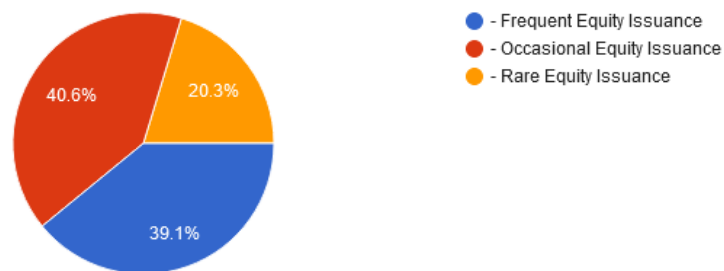


Figure 15: Common trends in equity issuance among LLCs and their impact on cost of capital

The most common response among respondents is the preference for occasional equity issuance, with 40.6% selecting this option. Respondents favouring occasional equity issuance probably view it as a strategic tool for specific situations, such as funding major projects, expansions, or addressing capital needs without being a regular practice. A close second in popularity is the option for frequent equity issuance, with 39.1% of respondents selecting this trend. Those favouring frequent equity issuance may see it as an ongoing strategy to fund operations, projects, or to maintain flexibility in capital structure. This approach could indicate a proactive stance toward capital-raising opportunities. A minority of respondents (20.3%) indicated a preference for rare equity issuance. Respondents in this category may prefer to rely on other financing sources and use equity issuance sparingly. This could suggest a focus on maintaining ownership control or avoiding dilution of existing shareholders.

The distribution of responses suggests a significant variability in the strategic approach to equity issuance among LLCs. Each approach may be driven by unique organizational needs, industry dynamics, or growth plans. The prevalence of occasional and frequent equity issuance suggests that LLCs recognize the need for flexibility in their financing strategies. This allows them to adapt to changing market conditions, business opportunities and capital requirements. The chosen frequency of equity issuance probably aligns with broader organizational strategies

and goals. Frequent issuers may prioritize agility, while occasional issuers may emphasize control and stability. The frequency of equity issuance may be influenced by market conditions, with organizations adjusting their strategies based on the availability and cost of capital in the market. The chosen approach may be indicative of the LLCs' current growth trajectory. Frequent issuers may be in a rapid expansion phase, while occasional issuers may be focused on sustaining existing operations. The responses suggest that LLCs are willing to adapt their capital structure based on their specific needs and the prevailing economic and market conditions.

6. How does the ownership structure typically influence the cost of capital for LLCs?

133 responses

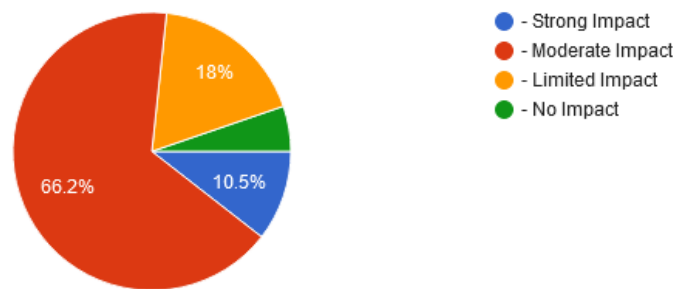


Figure 16: Impact of ownership structure on cost of capital for LLCs

In terms of the effect of ownership structure on cost, (66.2 %) think that there is a moderate influence on capital for LLCs. From this we can deduce that most respondents realize that the structure of capital ownership has an effect on the cost of capital, but don't believe it is an only determining factor. Besides the ownership structure factors, including market conditions, industry dynamics and financial policies are probably also regarded as important. Another smaller percentage (18 %) of respondents, however, believe the effect of ownership structure on cost of capital is very limited. Those in the former group might well consider that such objects as cost of capital, business operations, financial management and market conditions are more significant than ownership structure. Only a small percentage of respondents (10.5 %) believe that the cost of capital is strongly affected by the ownership structure. This subset of respondents probably sees ownership structure as a critical factor influencing the cost of capital. Changes in ownership may be viewed as having a significant effect on the financial dynamics and risk profile of the business. Only a minority of respondents (5.3 %) holds that ownership structure has no relation to the cost of capital. In fact, this group may see ownership structure as having no connection to financing decisions and other variables that affect cost of capital.

Responses show that respondents are aware of the complex nature of factors affecting the cost of capital. While ownership structure is considered, it is not viewed in isolation from other critical elements. Since the impact is considered moderate, this indicates that other factors are

weighed along with the ownership structure in calculating the cost of capital for LLCs. Those indicating a strong impact may have a heightened perception of the risks associated with changes in ownership, leading them to believe it significantly affects the cost of capital. Respondents anticipating changes in ownership may need to closely monitor and manage the associated impacts on the cost of capital. As business strategies evolve, the perceived impact of ownership structure on the cost of capital may also change. Continuous monitoring with additional assessment will be necessary. The responses suggest a need for adaptive and flexible financial planning which would allow LLCs to adjust their financing strategies based on changing ownership structures and broader business dynamics.

7. In your experience, how do prevailing market conditions commonly impact the cost of capital for LLCs?
133 responses

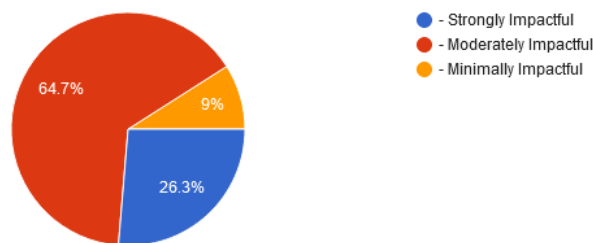


Figure 17: Impact of prevailing markets on cost of capital in LLCs

Most respondents (64.7%) feel that influence of existing markets have a moderately impactful influence on the cost of capital for LLCs. This indicates that a majority of respondents realize the influence of market conditions on the cost of capital. Market dynamics, interest rates and investor sentiment are probably considered significant factors in financial decision-making. A relatively high proportion of respondents (26.3 %) view the impact on cost of capital as being strongly influenced by prevailing markets. Those indicating a strong impact probably believe that market conditions have a pronounced and direct effect on financing decisions. Sometimes rapid changes in markets trigger adjustments to capital structure and funding policies. The minority of respondents (9%) respondents believe that existing markets are very minimally influential on cost of capital. The respondents of this type are more likely to minimize the impact of market conditions and focus on other factors like operational efficiency or long-term financial management.

The results show that generally respondents expressing a general sensitivity to market conditions among respondents, even though the degree of impact varies. The recognition of moderately or strongly impactful market conditions suggests that LLCs are attuned to the dynamic nature of financial markets and their potential impact on financing decisions. The prevalence of moderately or strongly impactful responses suggests that LLCs in flexible

financial planning, changes accommodation strategies according to the market environment. Respondents indicating a strong impact may prioritize proactive risk management, responding swiftly to market changes to mitigate potential adverse effects on the cost of capital. This view can vary over time with changes in economic conditions, interest rates and general market. Continuous monitoring will be necessary. The impact on the cost of capital may actually be related to global or local market conditions. But global trends and regional market conditions may force adjustments. The responses highlight the importance of scenario planning, allowing LLCs to prepare for various market conditions and adjust their financial strategies accordingly.

8. Are there industry trends that you believe universally affect the cost of capital for LLCs?

133 responses

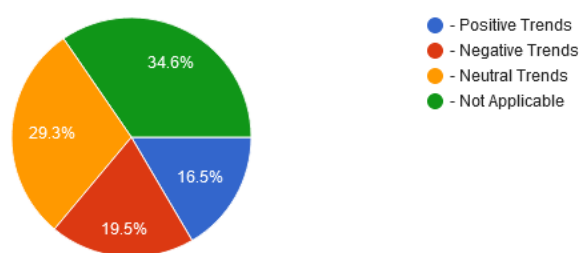


Figure 18: Industry trends affecting cost of capital in LLCs

The highest proportion of respondents (34.6 %) said that industry trends do not affect their LLCs' cost of capital. Respondents in this group may be involved in industries for which decision-making about financing is not greatly affected by industry trends. Or, perhaps they have business models or approaches that differ so much from everyone else's that industry trends don't apply. Some respondents (29.3 %) considers that the influence of these industry trends on cost of capital is neutral. From this we can infer that some respondents see industry trends as not having much of an impact on the cost of capital. This could be said to represent a balanced or negligible effect. However, an even smaller proportion of respondents (19.5 %) feel that the deteriorating in industries affects the cost of capital. Those showing negative tendencies might well be aware that negative changes in their industry create problems for obtaining capital, which affects decision-making about risk evaluation and debt structures. A minority of respondents (16.5%) sees positive industry trends as impacting the cost of capital. Only 16.5 % believes that positive industry trends affect the cost of capital. Respondents belonging to this group believe that advantageous industry conditions can trigger strategic financing, which will lower costs of capital or increase accessibility of funds.

The diversity of response shows that the level of influence of industry trends on cost of capital differ with different types of LLC. Respondents may weigh the potential impact of industry trends against other factors besides industry trends when making financing decisions.

The prevalence of "not applicable" responses underscores the importance of industry-specific strategies. Some businesses might have to address these problems by adjusting their financial plans according to the natures of their industries. Those respondents who admitted to neutral, positive or negative trends manifest the necessity for flexible financial planning based on taking account of an industry's particular difficulties and advantages. Continuous monitoring of industry dynamics will be important for LLCs, especially those indicating a direct impact of trends, to adjust their financing strategies in response to changing circumstances. Changes in the competitive landscape and emerging industry trends may prompt LLCs to reassess their cost of capital and financial strategies. Given the diverse responses, scenario planning based on various industry trends and developments will be important for LLCs to remain flexible in their financial decision-making.

9. How do industry-specific factors typically influence the cost of capital for LLCs?
133 responses

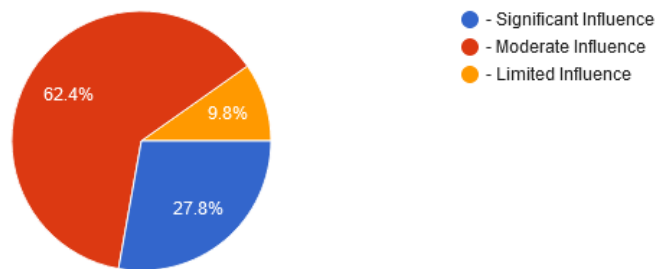


Figure 19: Influence of industry-specific factors on cost of capital for LLCs

27.8% of respondents think industry-related factors have a great bearing on the cost of capital for LLCs and this shows that a significant number of people are aware of the influence of industry-related factors on financing decisions. The cost of capital is likely critically influenced by such factors as industry trends, regulations and competitive factors. Most percentage of respondents (62.4%) sees industry-specific factors as having a moderate influence on the cost of capital. Perhaps those who answer a moderate degree of impact understand the essential significance of industry environment, but feel it is also possible that other external or internal factors can have an influence on financing decisions. A small minority of respondents (9.8%) thinks that industry-specific factors have a limited influence on the cost of capital. Perhaps these respondents feel that the influence of industry-related aspects is weaker than other considerations like overall economic conditions, or company-level financial management practices.

The responses where respondents indicated significant influence suggests that industry-specific factors are highly sensitive and influential in determining the cost of capital for LLCs. Businesses probably factor in industry-specific nuances when formulating their financial strategies and managing their capital structure. The 27.8% recognizing significant influence

highlights the need for industry-centric financial strategies. Apparently, businesses must coordinate their investments in finance with trends within an industry, regulations and competitive conditions. It would appear that an awareness of industry-specific factors is rising in status. Ongoing observation of industry-related factors will be crucial for LLCs to fine tune their financial strategies to the changing nature of their particular line of operation. If industry competitiveness, government regulations or technology change, LLCs will have to re-evaluate their cost of capital and strategic planning. Answers of respondents indicated that, adaptive financial planning that incorporates industry-specific considerations will be essential for LLCs to navigate the challenges and opportunities within their sectors.

10. What are the common expectations regarding returns and how do they impact the cost of capital?

133 responses

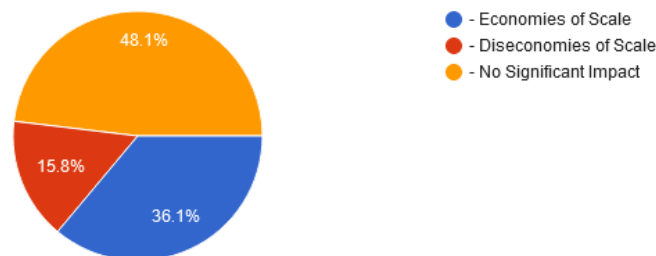


Figure 20: Expectations regarding returns and their impact on the cost of capital

The largest percentage of respondents (48.1%) believes that expectations regarding returns have no significant impact on the cost of capital for LLCs. From this we can see that the group of respondents admit that returns are not the most important consideration when looking at cost of capital. Other factors, such as operational efficiency or market dynamics, may be seen as more important. A lesser portion of the respondents (36.1 %) still believe that economies of scale may affect cost of capital. Those expecting economies of scale may believe that as the scale of operations increases, there will be cost efficiencies that positively influence the cost of capital. Only 15.8 % of respondents believe that diseconomies of scale will affect the cost of capital. Respondents in this category may expect that as the scale of operations increases, there could be inefficiencies or increased costs that negatively impact the cost of capital.

Their responses have revealed the range of demands on the relationship between returns and cost of capital. Also, opinions on how scale affects company funding differ according to the business. The abundance of “No significant impact” answers indicates that many LLCs do a comprehensive job, taking into account other issues in addition to return in calculating their rate of capital. Those expecting economies or diseconomies of scale to impact the cost of capital probably emphasize the importance of scale-related factors in their financial decision-making. For those anticipating economies of scale, ongoing efforts to enhance operational efficiency will

be important to realizing the expected positive impact on the cost of capital. Businesses expecting diseconomies of scale may need to implement risk mitigation strategies in order to address potential problems that may be associated with increased operational scale. Given the diverse expectations, LLCs may need to maintain adaptive financial strategies that can accommodate various scenarios related to returns and operational scale.

11. Based on your experience, how has historical financial performance commonly influenced the cost of capital for LLCs?

133 responses

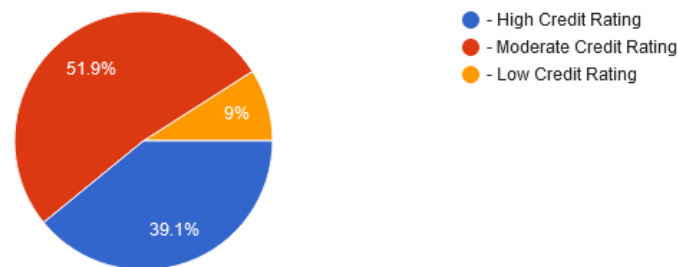


Figure 21: Influence of historical financial performance on cost of capital in LLCs based on respondents' experience

Most respondents (51.9 %) believed that historical profitability and the performance of the company has led to a moderate credit rating, which affects the cost of capital. This may show us that a significant portion of respondents perceives their financial performance as having a moderate impact on their credit rating, which in turn influences the cost of capital. A moderate credit rating indicates a balance between risk and steadiness. A smaller amount of respondents (39.1 %) said that a high credit rating based on their historical financial performance. Those with a high credit rating probably benefit from a strong financial track record, leading to lower perceived risk by lenders and potentially resulting in a lower cost of capital. Only (9 %) said their credit rating was low, based on previous performance. However, lenders could find it difficult to evaluate respondents in this category due to uncertainties about creditworthiness, leading them to perceive a higher degree of risk and a consequent increase in the cost of capital.

The distribution of responses highlights variability in the perceived credit ratings among respondents, reflecting diverse financial situations and performance levels. From the distribution of credit ratings, it appears that LLCs are deliberately seeking an appropriate balance between risk and return. Low or high credit ratings may be more indicative of risk profile, while moderate scores are suggestive of a pragmatic approach. However, for those with a modest or low credit scores it will remain essential to continue striving for greater improvement in performance and credit status so as to secure an even more favorable rating in the future. Even businesses with good credit ratings might have to keep watch on risk everywhere in order to preserve their

current status. These responses show that financial planning must be flexible, so that they can respond in line with the way their financial behavior improves or deteriorates.

12. What are the typical considerations in assessing the impact of future plans on the cost of capital?

133 responses

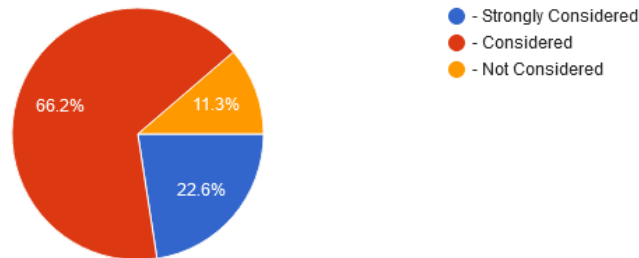


Figure 22: Typical considerations in assessing the impact of future plans on cost of capital

Most respondents (66.2%) reported that typical considerations in assessing the impact of future plans are considered in the determination of the cost of capital. This indicates that a significant portion of respondents actively takes future plans into account when making decisions about their cost of capital. Changes in business strategies, diversifications and expansions could be included in future plans. Significant but still less respondents (22.6%) reacted to the question in the way that future plans are strongly considered in the assessment of the impact on the cost of capital. Those strongly considering future plans probably place a higher emphasis on the role of strategic initiatives in shaping their cost of capital. This suggests that future plans play a central role in financial decision-making. A minority of respondents (11.3%) reported that typical considerations in assessing the impact of future plans are not considered in the determination of the cost of capital. Respondents in this category may prioritize other factors or believe that future plans have limited relevance in shaping their financing decisions and determining the cost of capital.

The prevalence of "considered" and "strongly considered" responses indicates a general alignment between future plans and the determination of the cost of capital, reflecting a strategic and forward-looking approach among respondents. The majority considering future plans suggests that many LLCs integrate their strategic initiatives and future plans into the fabric of their financial decision-making processes. For those strongly considering future plans, clear communication of these plans to stakeholders and potential investors may be important, as these plans significantly influence the cost of capital. Given the dynamic nature of business environments, LLCs may need to continuously assess and adapt their financial strategies based on evolving future plans. The consideration of future plans may benefit from scenario analysis, allowing businesses to evaluate the potential impact on the cost of capital under various strategic

scenarios. The responses highlight the importance of adaptive financial planning, enabling LLCs to adjust their cost of capital strategies in response to changes in future plans and business strategies.

13. How does the current tax environment commonly impact the cost of capital for LLCs?
133 responses

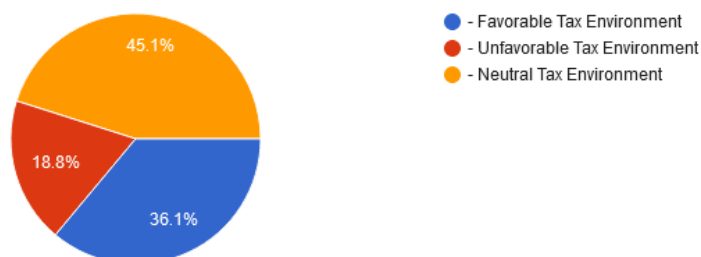


Figure 23: Impact of current tax environment on cost of capital in LLCs

In terms of the cost of capital, (45.1%) view the current tax environment as neutral to that for LLCs. This means that a significant portion of respondents admits that the current tax environment neither significantly decrease nor increase the cost of capital, implying a balanced situation. However, responding to the question of whether tax policy is beneficial or detrimental to cost of capital respondents' view the current tax environment as favourable to the cost of capital. A substantial but smaller percentage of respondents (36.1%) view the current tax environment as favourable to the cost of capital. Respondents that believe in favourable tax environment probably believe that current tax conditions create a positive impact on the cost of capital, possibly by reducing tax liabilities or providing incentives. A minority of respondents (18.8%) believes that the current tax environment is unfavourable to the cost of capital. Participants in this group perhaps feel that the current environment forces them to face difficulties or increases their tax burden, thus adversely affecting their cost of capital.

The distribution of responses highlights variability in how respondents perceive the impact of the current tax environment on the cost of capital. Neutral responses tell us that many LLCs practice adaptive tax planning, strategizing the way they do taxes according to the current environment without feeling that they're favoring one or other side. Those seeing a positive tax climate may also see opportunities for strategic management of taxes to optimize the cost of capital. However, respondents who feel they are in an unfavorable tax environment have to take countermeasures for risks arising from the tax environment and have to find ways to optimize the cost of capital while within the limitations of the tax environment. Since tax policies are changing rapidly, perhaps in the future LLCs should pay particular attention to any change in regulations that may affect their cost of capital. Future planning based on different tax zones contains a prepared plan that will enable business to face undefined changes in the tax

environment and mitigate the future risks and approximately estimate their impact on the cost of capital. The responses highlights the importance of tax-responsive financial strategies, allowing LLCs to navigate different tax environments while optimizing their cost of capital.

14. Are there specific tax incentives or liabilities that commonly influence financing decisions for LLCs?

133 responses

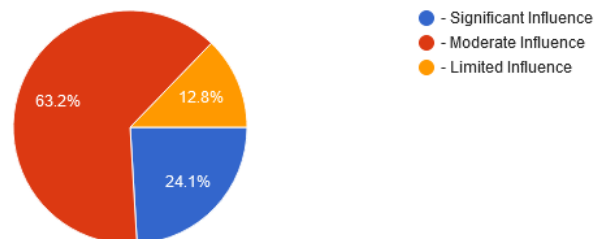


Figure 24: Influence of specific tax incentives or liabilities on financing decisions in LLCs

Most respondents (63.2%) responded that specific tax incentives or liabilities have a moderate impact on LLC's financing decisions, hence, a significant portion of respondents admit the importance of tax-related considerations in shaping financing decisions but does not view them as overwhelmingly determinative. A smaller percentage of respondents (24.1%) believe that some tax incentives or liabilities have a significant influence on the financing decision. Respondents of this group prioritize tax-related factors as key determinants in their financing decisions. Specific tax incentives or liabilities may play an important role in planning their future financial decisions. Only 12.8 % of respondents consider specific tax incentives or liabilities to have little effect on financing choices. Perhaps respondents in this category think that these other factors, like market conditions or operational considerations are stronger drivers of financing decisions and tax-related factors do not carry as much weight.

The fact that the numbers for moderate and high influence are highest suggests that people incorporate tax considerations into the process of making a decision, but do not necessarily take them as decisive factors. The majority which admits a moderate influence suggests that LLCs often balance tax considerations with other factors when making financing decisions, aiming for a strategic approach. Those who indicate this is important may well rely on tax planning as part of their overall financial strategy, either to seek out incentives or minimize liabilities. People who recognize a strong influence must take steps to manage their taxes, so as to structure financing as effectively as possible in consideration of the current tax situation. Those acknowledging a significant influence may need to engage in constant and cautious tax management to optimize financing decisions based on the existing tax environment. Responses like this reflect the necessity of financial flexibility capable of adapting to different variations in

tax incentives or obligations. The responses highlight and show us that the need for adaptive financial strategies that can adapt to changes in tax incentives or liabilities, ensuring that financing decisions remain the same with overall business goals.

15. In your experience, how does compliance with regulations typically impact the cost of capital for LLCs?

133 responses

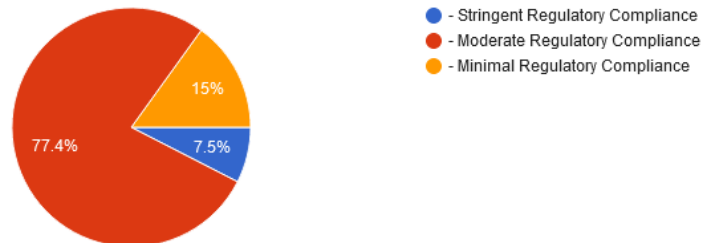


Figure 25: Impact of compliance with regulations on cost of capital in LLCs based on the experience of respondents

Most people (77.4 %) responded that moderate regulatory compliance does indeed moderate influence to the cost of capital. From this we can see that most respondents understand the need to take government regulations seriously but do not find them impossible or too strict. But only a minority of respondents (15 %) thinks that poor regulatory compliance affects the cost of capital. Bearing in mind industry and operating conditions, respondents falling in this group may believe that regulatory compliance has little impact on the cost of capital. Only a small minority (7.5 %) sees stringent compliance with regulations as affecting the cost of capital factor. Of course, it raises costs and affects the cost of capital in an LLC.

The distribution of responses can show us the variability in how respondents consider the impact of regulatory compliance on structuring the cost of capital. High number of moderate compliance responses suggests that many LLCs aim for a balanced approach to regulatory compliance, recognizing its importance without viewing it as overly burdensome or minimal. The divergent reactions illustrate that attention must be paid to industry-specific regulatory environments, as compliance requirements may vary significantly across different sectors. Because regulatory compliance affects the cost of capital, businesses will have to pay close attention to the changes in the regulations and adapt to them constantly. For those acknowledging stringent compliance, active strategies may be essential to minimize adverse effects on the cost of capital. These answers prove that there must be some flexible compliance measures used to adapt to changes while maintaining the optimal level of possible cost of capital.

16. Are there specific regulatory requirements that are commonly considered in financing choices for LLCs?

133 responses

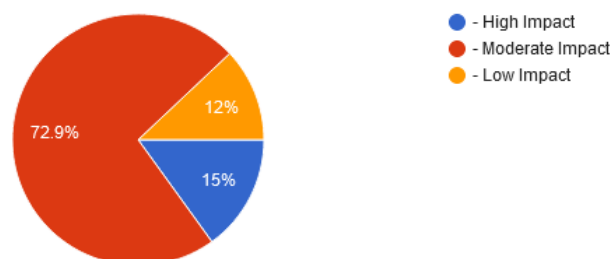


Figure 26: Specific regulatory requirements considered in financing choices in LLCs

Most respondents (72.9 %) said that certain legal regulations have a moderate impact on the financing decision in LLCs. Suggesting that the majority of respondents is aware of the effect of regulation standards on financing choices but does not see this as a determining factor. Almost fifth of respondents (15 %) feel that specific regulatory requirements have a relatively great impact on financing decisions. Those indicating a high impact probably consider regulatory compliance as an important factor in shaping their financing decisions. Special regulations can have a deep impact on the way financial arrangements are organized. A minority of respondents (12%) see certain regulatory requirements as having a low impact on their financing decisions. Respondents in this category may view other factors, such as market conditions or strategic considerations, as more decisive in financing choices, referring regulatory requirements to a secondary role.

The prevalence of moderate impact responses can show us that majority of LLCs should have a balance between regulatory compliance and other factors when making financing choices and reach optimal financial decision. The majority admit a moderate impact indicates that LLCs engage in comprehensive decision-making, considering regulatory requirements alongside other strategic and financial factors. Respondents indicating a high impact, strategic regulatory risk management may be important in optimizing financing choices and ensuring compliance with specific requirements. Given the potential impact of regulatory requirements, LLCs may need to stay in the same line of changes in regulatory environment that could affect financing decisions of management in the future. The responses highlight the importance of adaptive strategies that can adapt to changes in specific regulatory requirements while optimizing financing decisions. The analysis underscores the need for adaptive financial planning that considers the relations between regulatory requirements and financing choices.

17. How do industry-specific factors typically influence the cost of capital for LLCs?

133 responses

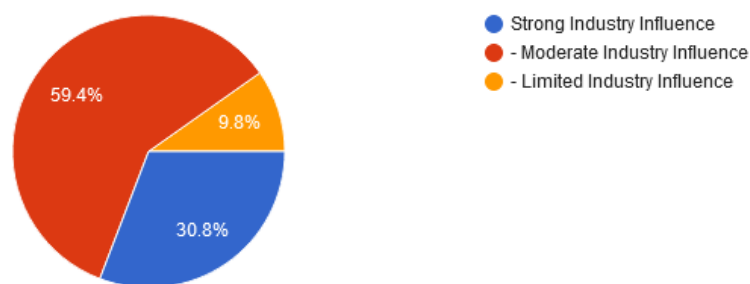



Figure 27: Influence of industry-specific factors on cost of capital in LLCs

The majority of respondents (59.4%) indicated that industry-related factors have a moderate influence on the cost of capital in LLCs. What this says is that a large proportion of respondents understand the role played in cost of capital by industry characteristics but not to an extent where they consider these factors mostly determinative. Smaller percentage of respondents (30.8%) believes that industry-specific factors have a strong influence on the cost of capital. Those indicating strong industry influence probably consider industry-specific factors as key determinants in their cost of capital, reflecting a higher sensitivity to sector-specific conditions. Industry-specific factors are seen by only a minority (9.8 %) of respondents as having very little impact on the cost of capital. Respondents in this category may view other factors, such as general economic conditions or internal financial management, as more decisive in determining the cost of capital, also considering as an industry-specific factors to a secondary role.

The large proportion of moderate industry influence responses indicates that when most LLCs decide on their cost of capital, they do not see extreme advantages or disadvantages and there is a balance should be preserved between industry-specific factors and other considerations when determining their cost of capital. The majority recognizing moderate industry influence indicates that LLCs often engage in holistic decision-making, considering industry-specific conditions alongside broader financial and economic factors. For those indicating strong industry influence, industry-centric financial strategies may be important in optimizing the cost of capital based on the unique characteristics of their sectors. But industry-specific factors could well influence the cost of capital in future, so perhaps LLCs must constantly keep an eye on changes in the overall industry environment to look out for tomorrow. The responses highlight the importance of possible strategies that can adapt to changes in industry-specific factors while preserving the optimal level of the cost of capital. The analysis emphasized the need for flexible financial planning that takes into consideration changing relationships between industry-related variables and the cost of capital.

18. Are there competitive dynamics within industries that commonly impact financing decisions for LLCs? 
133 responses

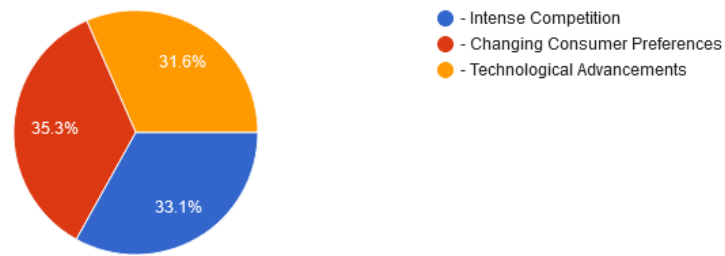


Figure 28: Competitive dynamics within industries impacting financing decisions in LLCs

The greatest number of respondents (35.3%) said that attention to changing consumer tastes influences financing in LLCs. It would seem that a majority of respondents are already aware they should get their financing decisions in line with changes in consumer choice, which perhaps reflects an approach to finance firmly based on the consumer. A smaller percentage of respondents (33.1%) believes that intense competition impacts financing decisions. The ones who say there is a strong internal competitive effects are probably more prone to strategic financial decisions that consider the competitive environment or maintaining competitiveness in the market. Another significant number of the respondents (31.6 %) acknowledges that technological development has an impact on financing choices. These respondents must see technology as a force at the core of business decision-making, with finance decisions being organized to make use of or keep up with technological changes.

Comparisons of the answers give some clue to how competitive relations in industry are multipronged, with changing consumer habits, competitive pressures and technological progress all seen as significant factors. Those with the highest percentages for impact say changing consumer preferences make businesses understand that there is a great need to coordinate financial and business behavior with consumer trends and needs. For those emphasizing intense competition, financial decisions probably prioritize strategies that enhance competitiveness, such as pricing, marketing, or innovation. The high proportion of people who assign significance to technological change indicates some level of understanding about how technology is steering the world and financial investments being taken in anticipation of adopting and using new technological developments in order to gain advantages. Of course, changing consumer demand, competition and technology may all require businesses to constantly check out the condition of the market. The responses highlight the importance of adaptive financial strategies that can adapt to changes in competitive dynamics, consumer preferences and technological environment. The

analysis highlights how competitive forces within an industry are multi-faceted and that appropriate financial planning should adjust in response to the business environment.

19. From your perspective, how do external economic factors, such as interest rates and inflation, commonly impact the cost of capital for LLCs? [Copy](#)

133 responses

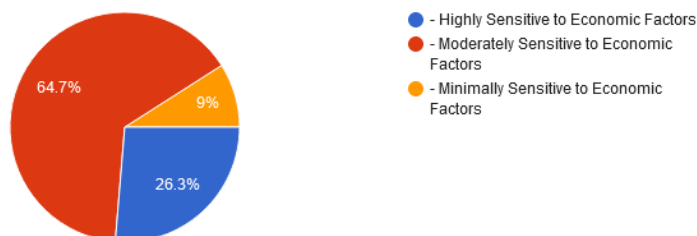


Figure 29: Impact of external economic factors (e.g as interest rates and inflation on cost of capital in LLCs)

In fact, most (64.7 %) respondents indicated that the cost of capital is quite sensitive to external economic factors like interest rates and inflation. This indicates the majority of respondents appreciate the impact of objective economic conditions, yet do not see them as decisive factors affecting cost of capital. A substantial but smaller percentage of respondents (26.3%) feel that external economic factors can directly have a great influence on the cost of capital. Respondents which indicate high sensitivity probably prioritize closely monitoring and adapting financial strategies in order to quickly respond to unexpected changes in interest rates, inflation and other external economic factors that could significantly influence the cost of capital. Only (9 %) of respondents sees external economic factors as little sensitive to the cost of capital. By contrast, respondents in this category perhaps feel that other factors - such as factors or the conditions of the industry concerned - have more to do with cost of capital, hence, pushing external economic factors into second place.

Responses are spread out across the spectrum, which suggests that people have different views as to whether the cost of capital is sensitive to external economic conditions. The majority recognize their dependency on the moderate sensitivity of external economic conditions, it can be inferred that many LLCs adopt a balance between internal and external factors. For those indicating high sensitivity, constant high level economic management may be important, involving continuous monitoring and swift responses to changes in interest rates and inflation to optimize the cost of capital. Given the perceived sensitivity, businesses may need to engage in regular economic forecasting to anticipate and respond to changes in external economic conditions that could impact the cost of capital. Considering different economic scenarios may help businesses prepare for potential changes in interest rates and inflation, allowing for more informed financial decision-making. The responses show us the need for adaptive financial

planning that considers the dynamic nature of external economic factors, in order to adjust accordingly to changes in the external economic conditions that will affect the cost of capital.

20. Are there specific external economic risks that are commonly considered in financing decisions for LLCs? [Copy](#)

133 responses

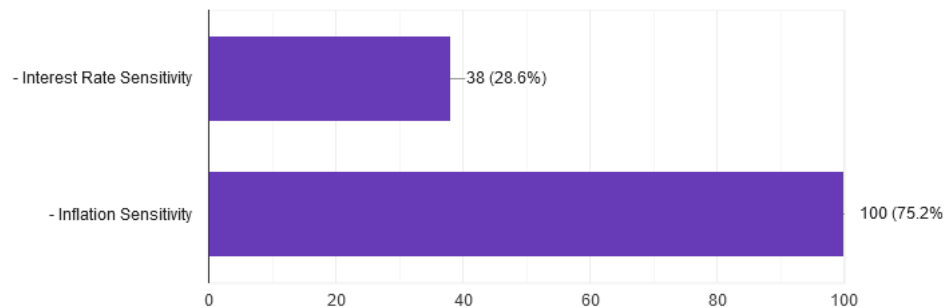


Figure 30: External economic risks considered in financing decisions in LLCs

The question in Figure 30 is multiple choice question, one person can choose more than one answer. More than three-fourths (75.2%) indicated that inflation sensitivity is considered in financing decisions in LLCs. This suggests that a significant portion of respondents recognizes the impact of inflation on financing decisions, indicating an active approach to managing inflation-related risks and optimizing financial strategies accordingly. A smaller percentage of respondents (28.6%) believe that interest rate sensitivity is considered in financing decisions. Those indicating interest rate sensitivity probably prioritize monitoring and managing interest rate-related risks, adjusting financing decisions in response to changes in interest rates to optimize their financial strategies.

The responses suggest that there are differences in the way people view particular specific external economic risks in financing decisions. This indicates that businesses understand the effect of financing decisions on inflation sensitivity and are willing to adopt management methods for handling risks from inflation. For those emphasizing interest rate sensitivity, strategic interest rate risk mitigation measures may be essential in optimizing financing decisions and protecting against interest rate fluctuations. Given the perceived significance of inflation and interest rate sensitivity, businesses may need to engage in scenario planning to assess the potential impact of different economic scenarios on their financing decisions. Constant monitoring and assessment of inflation and interest rate risks may help businesses stay proactive in adjusting their financing strategies based on changes in external economic conditions. The responses show the need for adaptive financial planning that is responsive to the specific external economic risks, allowing businesses quickly as well as effectively respond to changes in inflation and interest rates.

21. In your opinion, who are the key decision-makers in determining the capital structure for LLCs?

133 responses

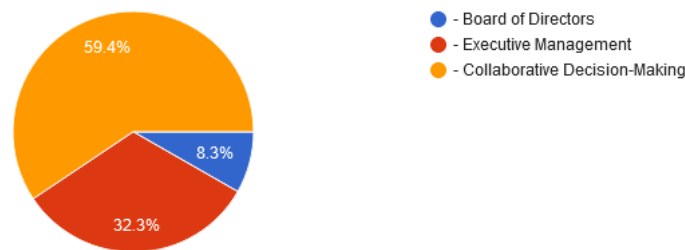


Figure 31: Key decision makers in determining capital structure of LLCs according to respondents

Most respondents (59.4 %) felt that collaborative decision making is most important in influencing the capital structure of LLCs. This suggests that a significant portion of respondents favours a collaborative approach involving input from various stakeholders in the decision-making process related to capital structure. This approach probably integrates insights from different functional areas within the organization. Similarly, a smaller proportion of respondents (32.3 %) regard executive management as the decisive factor on capital structure. Those attributing decision-making to executive management probably accent the importance of leadership and senior management in shaping the financial structure of the LLC, indicating a more top-down decision-making process. Only 8.3 % of the respondents see the board of directors as the final decision-maker in capital structure decisions. Such respondents are more likely to consider the role of the board as a kind of supervisory function, whose ignition largely depends on collective or executive control over capital structure.

The dominance of collaborative decision-making responses indicates a preference for inclusive and collaborative processes in determining the capital structure. The high proportion attributing importance to collaborative decision-making suggests that many LLCs prioritize a holistic approach, involving various stakeholders in the decision-making process to capture diverse perspectives. For those emphasizing executive management, strategic decision-making probably involves strong leadership influence, with executive management guiding the financial strategy of the LLC. While a minority, those recognizing the board of directors may view its role as providing oversight and strategic guidance in the capital structure decision-making process. With this kind of collective decision so common, companies might need to strengthen cooperation and coordination among relevant departments and interests in order to achieve the best possible decisions about capital structure. Of course, if the focus is on executive management, then building leadership cultivation may be necessary to promote sound decision making and strategy implementation. The analysis highlight the need for adaptive decision-

making models that can consider collaborative approaches while recognizing the influence of executive management and board oversight in determining the capital structure.

22. How do internal dynamics and decision processes commonly influence the cost of capital?

133 responses

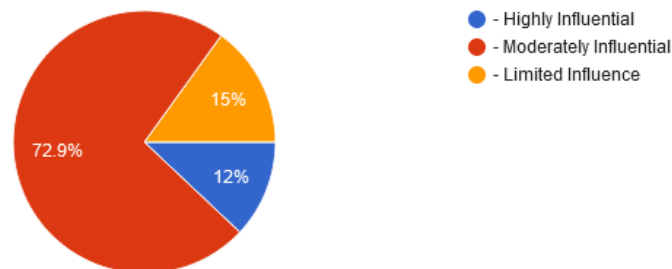


Figure 32: Influence of internal dynamics and decision processes on cost of capital

As for the influence of internal factors, 72.9 % said that they have only a moderate impact on cost of capital. That indicates that a huge amount of respondents are aware of internal factors influencing the cost of capital, but does not consider them all-determining. A minority of respondents (15 %) consider internal factors and decision-making as having only limited impact on the cost of capital. Respondents in this group perhaps place more emphasis on external elements, such as industry trends, the market or financial conditions, when calculating the cost of capital. The 12% of respondents think that the process of decision-making and internal dynamics affect cost of capital. Those indicating high influence probably attribute a significant portion of the cost of capital to internal factors such as organizational structure, efficiency, or strategic decision-making processes.

The allocation of responses can show us a balanced perception regarding the influence of internal dynamics and decision processes on the cost of capital. The majority recognizing a moderate influence suggests that many LLCs engage in comprehensive decision-making, considering internal dynamics alongside other external and industry-specific factors. For the respondents that think that there is only limited influence, strategic decisions may be more externally focused, with internal dynamics viewed as having a secondary impact on the cost of capital. Those indicating high influence probably prioritize optimizing internal processes and structures to positively impact the cost of capital, recognizing the importance of internal efficiency. Given the perceived influence of internal dynamics, LLCs may need to continuously assess and improve internal processes and decision-making to enhance their impact on the cost of capital.

Businesses may need to adopt an integrated approach, considering both internal and external factors in decision-making processes to optimize the cost of capital. The analysis underscores the need for adaptive financial strategies that consider both internal and external dynamics, allowing businesses to optimize their cost of capital in response to changes in organizational structures and decision processes.

CONCLUSION

Understanding the cost of capital for limited liability companies and what factors affect it can give us valuable insights into how these companies make financial decisions and manage their finances.

It's clear that the cost of capital for LLCs is shaped by a mix of internal and external factors. There are several internal elements such as financial health, risk exposure and growth potential of LLC and all these internal aspects are influencing on determining the cost of capital. Increased debt-equity proportion, decreased profitability and high market volatility tend to higher these costs. Whereas, strong cash flows a resilient balance sheet and favourable market perception can serve to reduce the cost of capital.

There are also several external factors that influence the cost of capital such as possible uncertainty in market or macroeconomic elements that can change the investor's risk perception (for example during economic instabilities and downturns investors' may try to look for higher returns) which will drive up the capital expenses of LLCs.

Optimal capital structure, balancing debt and equity, can help to decrease the cost of capital by optimizing the use of cheaper sources of funding. However, over reliance on debt or equity financing can also increase the cost of capital due to higher interest expenses or also the dilution of ownership.

Moreover, cost of capital of LLCs also depend on their industry, hence cost of capital may vary in different industries because different industries have unique risk profiles, growth rates and capital market expectations, resulting in varying cost of capital. Consequently, industry-specific factors should be also considered when analysing the cost of capital for LLCs.

In the study research methods tools both qualitative and quantitative, statistical analysis, graphical analysis, survey and content analysis are used. The object for the analysis is "GRANDMART" LLC – chain of supermarkets.

GrandMart's WACC, as calculated using different methodologies (Damodaran and Duff & Phelps), is around 12.47%, on average. This represents the required rate of return on both equity and debt for the company to attract and retain capital. The cost of equity is influenced by various factors, including the risk-free rate, equity risk premium, beta, small size risk premium, country risk premium and currency risk premium. In the case of GrandMart, the cost of equity ranges from 18.87% to 21.02%, reflecting the expected return demanded by investors for bearing the specific risks associated with the company and its operating environment in Azerbaijan. The cost of debt is influenced by the average interest rate for AZN-denominated borrowed funds and

the corporate income tax rate. For GrandMart, the pre-tax cost of debt is 10.00% and after-tax cost is 8.00%. This indicates the return required by lenders for providing debt capital to the company, with the tax shield partially offsetting the pre-tax cost. GrandMart's cost of capital is impacted by the country risk premium and currency risk premium, reflecting the risks associated with operating in Azerbaijan and having cash flows denominated in Azerbaijani Manat (AZN). These premiums contribute to the overall risk profile of the company and influence the cost of both equity and debt. The analysis indicates that both internal dynamics and external factors play a role in determining GrandMart's cost of capital. Factors such as company size, industry risk and market conditions contribute to the overall risk assessment. The survey results regarding key decision-makers in determining the capital structure of LLCs suggest a preference for collaborative decision-making in GrandMart. This inclusive approach involves input from various stakeholders, including executive management and collaborative decision-making processes. Respondents perceive internal dynamics and decision processes as having a moderate influence on the cost of capital for LLCs, including GrandMart. This balanced view suggests that while internal factors play a role, they are not the sole determinants of the cost of capital. The survey results indicate that industry-specific factors, economic uncertainties and market volatility are perceived as influential factors affecting the cost of capital for LLCs. For GrandMart, staying attuned to these trends and incorporating them into financial decision-making is vital. Survey responses highlight the significance of debt management strategies in influencing the cost of capital. GrandMart's WACC calculation reflects the impact of interest rates on the cost of debt and the overall cost of capital. GrandMart's cost of capital is influenced by the tax environment and regulatory compliance. The survey results emphasize the importance of considering tax incentives, liabilities and compliance in financing decisions.

The following suggestions can be made according to the research and analysis:

- The current capital structure need to be evaluated to ensure it aligns with the optimal mix of debt and equity. Given the importance of debt management strategies, consider refinancing options and debt instruments to minimize the cost of debt.
- Given the impact of country risk premium and currency risk premium on the cost of capital, GrandMart should actively manage and mitigate these risks. This could involve using financial instruments to hedge against currency fluctuations and staying informed about geopolitical and economic developments in Azerbaijan.
- GrandMart should stay attuned to industry-specific factors, economic uncertainties and market volatility. Regularly monitoring of economic trends in

Azerbaijan and the retail industry to proactively adjust financial strategies and capital structure in response to changing conditions are also required.

- GrandMart needs to explore options for diversifying sources of funding. This could include considering alternative financing methods, partnerships or accessing different financial markets to reduce dependence on a specific source of capital.
- Periodic reviews of the Weighted Average Cost of Capital (WACC) calculation need to be conducted. This will help ensure that the cost of capital reflects the most up-to-date information and market conditions, allowing for timely adjustments to financial strategies.
- It also needs to maintain a strong customer and market focus and respond to changing consumer trends and preferences to ensure sustained business growth, which, in turn, positively impacts the company's risk profile and cost of capital.

To sum up, GrandMart's cost of capital is influenced by a combination of internal and external factors, country-specific risks, economic conditions and collaborative decision-making processes. Understanding and effectively managing these factors are important for optimizing the cost of capital and making strategic financial decisions that align with the company's objectives and market conditions in Azerbaijan. Continuous monitoring of industry trends, economic developments and internal dynamics will be essential for adapting to changing conditions and maintaining a competitive cost of capital.

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APPENDIX 1 – SURVEY QUESTIONNAIRE

LLC Survey - demographic and awareness questions

Dear Respondent,

Thank you for participating in this survey. Your insights are valuable in this survey about Limited Liability Companies (LLCs). Please provide information in the first part of the survey and your awareness about LLCs:

1. What age category do you fall under?

- Between 25 - 35
- Between 36 - 45
- Between 46 - 55
- Above 55

2. What speciality category do you fall under?

- Finance and Accountancy
- Audit
- Executive Board

3. In which region of Azerbaijan do you currently reside?

- Baku, Absheron or Sumgayit
- Lankaran and surrounding regions
- Ganja and surrounding regions
- Guba and surrounding regions
- Shaki and surrounding regions
- Nakhchivan

4. What education category do you fall under?

- Secondary or High School
- Bachelor
- Masters
- PHD

5. How familiar are you with the term "Limited Liability Company" (LLC)?

- Very familiar
- Familiar
- Not familiar

6. Can you briefly describe the primary purpose or advantages of forming a Limited Liability Company (LLC)?

- Asset protection
- Pass-through taxation
- Limited personal liability
- All the above
- Not sure

7. Are you aware of the steps involved in forming an LLC?

- Yes
- No
- Partially

8. How would you define the concept of "cost of capital" as it relates to business finance?

- The overall cost of a company's funds
- The cost of debt and equity financing
- The return expected by investors
- Unsure

9. In your opinion, why is understanding the cost of capital important for individuals or businesses operating as Limited Liability Companies?

- Helps in making investment decisions
- Influences pricing and budgeting
- Affects profitability and growth
- All the above
- Unsure
- Not relevant to LLCs

LLC Cost of Capital Influencing Factors Survey

Dear Respondent,

Thank you for participating in this survey. Your insights are valuable in understanding the factors influencing the cost of capital for Limited Liability Companies (LLCs) in general. Please provide your opinions and feedback on the following aspects:

1. How do you perceive the influence of business structure on the cost of capital for LLCs? *

- Single-Member LLC
- Multi-Member LLC

2. In your opinion, what are the key risk factors that commonly impact the cost of capital for LLCs? *

- Market Volatility
- Industry-Specific Risks
- Economic Uncertainties
- Regulatory Risks

3. How do LLCs typically manage their debt obligations and what impact does this have on the cost of capital? *

- Conservative Debt Management
- Aggressive Debt Utilization
- Balanced Approach

4. To what extent do interest rates commonly affect the cost of capital for LLCs? *

- Highly Influential
- Moderately Influential
- Minimally Influential
- Not Applicable

5. Are there common trends in equity issuance among LLCs and how does this impact the cost of capital? *

- Frequent Equity Issuance
- Occasional Equity Issuance
- Rare Equity Issuance

6. How does the ownership structure typically influence the cost of capital for LLCs? *

- Strong Impact
- Moderate Impact
- Limited Impact
- No Impact

7. In your experience, how do prevailing market conditions commonly impact the cost of capital for LLCs? *

- Strongly Impactful
- Moderately Impactful
- Minimally Impactful

8. Are there industry trends that you believe universally affect the cost of capital for LLCs? *

- Positive Trends
- Negative Trends
- Neutral Trends
- Not Applicable

9. How do industry-specific factors typically influence the cost of capital for LLCs? *

- Significant Influence
- Moderate Influence
- Limited Influence

10. What are the common expectations regarding returns and how do they impact the cost of capital? *

- Economies of Scale
- Diseconomies of Scale
- No Significant Impact

11. Based on your experience, how has historical financial performance commonly influenced the cost of capital for LLCs? *

- High Credit Rating
- Moderate Credit Rating
- Low Credit Rating

12. What are the typical considerations in assessing the impact of future plans on the cost of capital? *

- Strongly Considered
- Considered
- Not Considered

13. How does the current tax environment commonly impact the cost of capital for LLCs? *

- Favorable Tax Environment
- Unfavorable Tax Environment
- Neutral Tax Environment

14. Are there specific tax incentives or liabilities that commonly influence financing decisions for LLCs? *

- Significant Influence
- Moderate Influence

- Limited Influence

15. In your experience, how does compliance with regulations typically impact the cost of capital for LLCs? *

- Stringent Regulatory Compliance
- Moderate Regulatory Compliance
- Minimal Regulatory Compliance

16. Are there specific regulatory requirements that are commonly considered in financing choices for LLCs? *

- High Impact
- Moderate Impact
- Low Impact

17. How do industry-specific factors typically influence the cost of capital for LLCs? *

- Strong Industry Influence
- Moderate Industry Influence
- Limited Industry Influence

18. Are there competitive dynamics within industries that commonly impact financing decisions for LLCs? *

- Intense Competition
- Changing Consumer Preferences
- Technological Advancements

19. From your perspective, how do external economic factors, such as interest rates and inflation, commonly impact the cost of capital for LLCs? *

- Highly Sensitive to Economic Factors
- Moderately Sensitive to Economic Factors
- Minimally Sensitive to Economic Factors

20. Are there specific external economic risks that are commonly considered in financing decisions for LLCs? *

- Interest Rate Sensitivity
- Inflation Sensitivity

21. In your opinion, who are the key decision-makers in determining the capital structure for LLCs? *

- Board of Directors
- Executive Management
- Collaborative Decision-Making

22. How do internal dynamics and decision processes commonly influence the cost of capital? *

- Highly Influential
- Moderately Influential
- Limited Influence