

Understanding the Nature of Capital Allocation Problem in Corporate Finance

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Abstract : One of the central problems in corporate finance is the allocation of funds. This usually takes two forms: allocation of funds across firms in an economy or allocation of funds across projects or business units within a firm. The first one is typically related to the external markets (the bond market, the stock market, banks and finance companies) whereas the second form of the capital allocation is related to the internal capital markets in which corporate headquarters allocate capital to their business units. (within-group transfers, within-group credit markets, and within-group equity market). The main aim of this study is to investigate the nature of capital allocation dynamics by comparing the relevant studies carried out on external and internal capital markets with paying special significance to the business groups.

Keywords : internal capital markets, external capital markets, capital structure, capital allocation, business groups, corporate finance

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