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The influence of the financial slack on the economical performance of Brazilian and Chilean companies

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Received 8 April 2016; accepted 29 December 2016

Abstract

Although financial slack is a resource used to generate opportunities, a high level of this may lead to a more relaxed or complacent management. Taking into account this divergence, the present study examines the influence of financial slack on economic performance. The study involved 190 companies in Brazil and 104 in Chile. The results indicate that in Brazil and Chile, the gross profit showed better explanatory power to the financial slack resources. However, the high discretionary financial slack showed negative magnitude and a positive link with the financial resources demand, suggesting that companies become proactive in new investments and in strategic choices when there is a demand for financial resources.

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La holgura financiera en el resultado económico de las empresas brasileñas y chilenas

Resumen

La holgura financiera es un recurso utilizado para generar oportunidades. Sin embargo, un nivel elevado de esta puede generar una gestión más relajada (o «acomodaticia»). Teniendo presente esta divergencia, este trabajo comprueba la influencia de la holgura financiera en el resultado económico de 190 empresas de Brasil y 140 de Chile. Los resultados indican que en los 2 países la holgura financiera presenta un mayor poder explicativo del beneficio bruto. En concreto, dicho beneficio bruto tiene una relación negativa con una elevada...
1. Introduction

Managing the financial slack is an alternative for fundraising, and an attractive way to leverage the business due to opportunities (Kim et al., 2008). Representing an excess of resources, the financial slack favors the overcoming of crises arising from the turmoil in the market, and allows investments in riskier projects and innovations, increasing the chances of favorable returns to organizations (Bradley et al., 2011a; Deephouse and Wiseman, 2000; Zona, 2012).

The excess of financial slack may cause the implementation and testing of new organizational projects (Bradley et al., 2011b; Zona, 2012), on the other hand, the shortage of funds forces managers to seek solutions to organizational problems that may be causing resource restrictions (Deephouse and Wiseman, 2000; Patzelt et al., 2008).

The financial slack can be a useful resource to the organization to assist in the achievement of organizational goals (Vanacker et al., 2013) and for the discretionary use of management. The discretionary financial slack is a continuum, ranging from high and low financial slack. The high discretionary financial slack, represents the net working capital, and the low discretionary financial slack, representing the degree of debt, becoming organizational investment options for managers. However, the higher the debt level, the lower the degree of management freedom, due to commitments (Bradley et al., 2011b; George, 2005). The funding restriction by organizations, can be combated by the liquidity management of cash flow, which becomes an issue for the corporate policy, and also affects organizational performance (Almeida et al., 2004).

In this context, it is assumed that the effective management of financial slack positively influences organizational performance (Bradley et al., 2011b; Simsek et al., 2007). However, if on the one hand, the slack increases the ability to take risks that influence innovation and consequently the performance of companies, on the other hand, high levels may favor the management accommodation or irrational optimism resulting in inadequate strategies for good organizational performance.

The cash balance policies are associated empirically to the value of the organization, growth opportunity, business risk and organizational performance (Acharya et al., 2007), and therefore, understanding the financial slack as an organizational resource, presents the following research issue: What is the influence of the financial slack in the economic performance of Brazilian and Chilean companies? Thus, this article aims at verifying the influence of the financial slack on economic performance of Brazilian and Chilean companies. Almeida et al. (2004) state that there are two important areas in corporate finance, which are the effects of the financial constraints on firm behavior and the way companies conduct financial management. With this approach, the present study addresses the financial management by companies and their impact on economic performance.

The companies selected for the study belong to Brazilian and Chilean capital market. The research is justified by the proposal of knowledge expansion regarding financial slack and its possible influence on organizational economic performance and whether there are significant differences between Brazilian and Chilean open market companies.

The choice of Chile is mainly given because it has greater global competitiveness index compared to countries in Latin America, and worldwide reaches the 33rd position, while Brazil ranks only 57th according to the World Economic Forum report (Schwab, 2015), making the country important in Latin America’s economic scenario and relevant to be compared to the Brazilian scene.

Moreover, Benachenhou (2013) highlights similarity features between Brazil and Chile, indicating that in reference to economic performance, organizations of both countries (Brazil/Chile) showed the best indicators. Specifically in Brazil in recent years, appeared in the world market as an agricultural power, and in the export of products in various industries. Chile is world known for the exportation of blueberries, grapes, plums, apples, pacific salmon, among others.

Brazil and Chile have gone through relevant economic, political and social transformations in recent decades, and became the most solidified Latin American economies (Bastos and Nakamura, 2009). Terra (2007) confirms that there is relevance to studies that include comparisons between Brazil and Chile, as they are emerging economies that have undergone major macroeconomic changes.

Finally, Brazil has achieved its goals of economic growth, strengthening the institution and improvement in income distribution in growing and democratic environment (Sicsú and Castelar, 2009). Similarly, Chile has been considered a reference in Latin America, as one of the few countries that coexists, with long periods with low inflation and economic growth (Rondinei et al., 2005). In addition, the Chilean economy is driven and open (Martinez et al., 2007), similar characteristic to the Brazilian market, plausible justification for comparison of listed companies on various aspects involving economic performance.

Based on Almeida et al. (2004), developing empirical propositions that cash flow policies determine investment
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