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WORKING CAPITAL MANAGEMENT AND PROFITABILITY

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ABSTRACT

This study investigates the impact of working capital management on the financial performance of selected cement companies in Tamil Nadu. The secondary data were collected from 10 companies for a five period from 2019 to 2024 the independent variables are current ratio, quick ratio and cash conversion cycle, while dependent variables included return on assets and net profit margin. Descriptive statistics, Pearson correlation, regression analysis were applied to examine the relationship between working capital management and profitability. The finding showed The CR and QR have a strong positive and significant relationship with return on asset and net profit margin, indicate that liquidity efficiency contributes to profitability, The CCC shows a negative but significant association with both measures of performance, highlighting the importance of maintaining an optimal cash cycle. The results confirm that effective management of working capital enhances financial performances and sustainability. The study concludes that financial managers must strike balance between liquidity and operational efficiency to achieve profitability and ensure long term growth in the cement industry.

KEYWORDS: Working Capital Management, Profitability, Liquidity, Cash Conversion Cycle, Company.

1.1 INTRODUCTION

Working capital management is prime aspect of financial management of the business. Every economy increases the quantity of investment not only in fixed assets also in working capital. The rate of growth of the business depends on the effective utilization of the working capital. The fund required for the daily operation have been variously called as short term finance The required capital for the business is based to fixed capital and working capital. Excess of

current assets over current liability is working capital. Its essential for day to day operations in organization.it s like life blood which flows through veins and arteries .the funds required for the short term purposes like to purchase the raw material ,wages to be paid and to meet day expenses and the funds required for to meet these expenses is known as working capital. Working capital is a part of firms capital which is financing for the short term current asset like cash marketable securities debtors and inventories.

It belongs to the short term funds needed for the operating cycle in business. The proper administration of working capital helps to identify to a extent of success or failure of the overall operations of an enterprise. The shortage of working capital is the main reason for the failure of business. The mismanagement of the resources of the firm transfigure the successful business into unsuccessful one. The working capital operates depend the credit days allowed by creditors and credit days given to debtors and stock of level to be maintained (Kosgey & Njiru, 2016.Firm must check on the working capital that they have adequate resources to meet the day to day operations(Runyora, 2012).The working capital levels of SME must be supervised because it has direct impact on the financial performance of their business(Owele, 2014).The main objective helps to avoid under or over investment in current assets .more investment in current assets reduces the profitability .Working capital management is important for finance .Gross working capital means current assets and net working capital means current assets minus current liability. The assets which is converted into cash within the one year. The current assets changes frequently. The smooth and fluent business operations is ensured by the current assets. The current assets are like stock, receivables, cash and bank balance. The current liabilities are paid off within the one year. Current liability are sundry creditors bill payable bank overdraft outstanding expenses.

1.2 REVIEW OF LITERATURE

Upreti and Venkata (2021) studied on the working capital strategies in Nepalese institutional schools in Central Development Region using 10 years 2008-2009 to 2017-2018 resulted that the institutions suffered from the lack efficient working capital management.

Pham et al. (2020) studied on the effects of working capital management on profitability of steel companies in Vietnam stock exchange using independent variables like DIO,DPO,DSO, CCC,SIZ,CR,LEV,GRO the data was collected for 20 companies for 10 years 2010-2019 and found DPO, DIO, DSO, CR, SIZ, GRO factors have positive impact on profitability and CCC and LEV has negative impact on profitability.

Hossain and Alam (2019). examined the relationship between liquidity and profitability between the firm using Pearsons correlation and found cash conversion cycle has strong negative relationship with profitability ratios (NPM,ROA and ROE).The liquidity ratios (CR and QR) had positive relationship with profitability ratios of the cement industry in Bangladesh.

Iqbal etal.(2014) studied on the link between the working capital management and profitability of Pakistan textile industry of 9 manufacturing firms for the year 2006-2012.Descriptive statistics ,correlation, regression are the statistical tools used found that current ratio and the cash conversion cycle has the negative effect on the firms profitability return on asset and net profit margin.

Ponsian etal(2014) examined on the effect of the working capital management on the profitability using the sample of 3 manufacturing companies in DSE for the period of 10 years 2002 -2012.The Pearsons correlation and the Regression analysis (Ordinary Least Square) is used found cash conversion cycle and average payable period has the positive significant impact on the profitability. The average collection period , liquidity inventory conversion period has the negative significant impact on the profitability. They suggested that only if the firm manages the cash receivable and inventories well the profitability of the firm will raise.

Gull (2013) assessed the relationship between the working capital and liquidity with firm performance. A sample of 19 cement companies were listed KSE for the period 2005-2010.using regression found that current ratio has significant relationship with return on capital employed thus increases the return on capital employed will also raise. The quick ratio is positive but has insignificant relationship with profitability both the inventory turnover ratio and average receivables ratios and oppositely connected that is decrease in these ratios raises the profitability and vice versa.

Javid and Zita(2014) investigated on the relationship between the working capital policy and firm profitability in cement sector listed in Indonesia Stock Exchange (IDX) for 2012-2017 for the six companies using partial least square used sobel test .they found that there is significant negative relationship between working capital policies on the profitability of the firms and working capital management has significant effect on the profitability of the firm.

1.3 Methodology

The study is to find the relationship of working a capital management and the profitability. The sample was 35 listed steel companies are taken for 5 years using 2017-2022.the dependent variable of this study is current ratio, quick ratio, average collection period, inventory conversion period ,average payable period and cash conversion cycle and the dependent variable is net profit margin. The descriptive statistics, Pearsons correlation and Regression are used using SPSS.

1.4 Hypothesis

H0: There is no relationship between the working capital management and net profit margin

H1: There is relationship between the working capital management and net profit margin.

1.5 Analysis and Interpretation

1.5.1 Descriptive Statistics

Table 1: Descriptive Statistics.

	CR	QR	ACP	ICP	APP	CCC	NPM
Mean	1.69	1.02	50.4	100.64	73.95	77.67	7.77
Standard Deviation	0.93	0.72	43.78	60.96	63.69	65.78	13.57
Kurtosis	3.46	3.34	10.23	2.94	4.82	2.52	5.56
Skewness	1.34	1.51	2.6	1.47	1.89	1.21	0.6
Minimum	0.23	0.13	2	13	1	-24	-51.21
Maximum	6.17	4.63	322	365	365	350	75.95
Count	175	175	175	175	175	175	175

Table 1 presents a summary descriptive statistics of dependent variable and independent variable for the 35 steel company listed in companys stock exchange for the period of 5 years from2017-2022.

It shows the mean of the current ratio and quick ratio is 1.69 and 1.02,the standard deviation is .93 and 72 respectively. The minimum values for current ratio and the quick ratio is 0.23 and 0.13.The mean of average collection period is 50.4 and standard deviation 43.78.The minimum and maximum values of the average collection period is 2 days and 322 days .it takes average 100 days to sell the inventory with standard deviation 60.96,maximum it takes 365 days to sell the inventory and minimum within 13 days .the firms takes average 74 days to pay their purchases with the standard deviation 63.69.the minimum time required is 1 day and maximum 365 days.

Table 2: Pearsons Correlation Analysis.

	CR	QR	ACP	ICP	APP	CCC	NPM
CR	1						
QR	0.861165	1					
ACP	0.134652	0.159397	1				
ICP	-0.06728	-0.20309	0.090771	1			
APP	-0.34037	-0.32187	0.234699	0.604264	1		
CCC	0.345665	0.220223	0.54169	0.439998	-0.21409	1	
NPM	0.299772	0.401894	0.11782	-0.03925	-0.0239	0.04707	1

Table-2 presents the Pearsons correlation used to find the relationship between working capital and net profit margin. Correlation between the working capital components show that the current ratio quick ratio average collection period average inventory period has the positive relationship significant relationship between the cash conversion cycle and negatively correlated with negative. The correlation between the cash conversion cycle and the profitability shows that the lengthening the cash conversion cycle lengthens the profitability.

Table 3: Regression Analysis.

Regression Statistics	
Multiple R	0.460986
R Square	0.212508
Adjusted R Square	0.184383
Standard Error	12.25773
Observations	175

The adjusted R2 of the model is 18.4 % and the value for R2 in the model 0.2125 which endorses that 21.25% of the variation in the dependent variable is explained by the model. The 78.75% variation in the dependent variable remains unexplained by the independent variables of the study.

Table 4: ANOVA.

	df	***SS***	***MS***	***F***	***Sig***
Regression	6	6811.741	1135.29	7.55	0.00
Residual	168	25242.31	150.2519		
Total	174	32054.05			

Table 5: Coefficient.

	Coefficients	*Standard Error*	*t Stat*	*P-value*
Intercept	-2.564	2.788	-0.919	0.359157
CR	-2.804	2.137	-1.311	0.191369
QR	11.123	2.678	4.152	0.000005
ACP	0.364	0.138	2.637	0.009149
ICP	0.361	0.139	2.593138	0.010349
APP	-0.323	0.133	-2.42892	0.016198
CCC	-0.349	0.133	-2.61372	0.00977

The result of regression indicates that the coefficient of ACP is 0.364 and the p value is 0.009149.the shows that the raise or reduction in ACP will significantly affects the profitability of the company. Since there is positive relationship between the average collection period and profitability to get more profitability the company should lengthen the average collection period days. The inventory conversion period coefficient highlighted that there is positive with 0.361 and p value of 0.010349.This states that when the ICP increases or decreases it significantly affects the firms profitability. The average payable period that the coefficient is the -0.349 and the p value 0.00977 showing that raise or reduction in the average payable period significantly affects the profitability of the company. There is negative relationship between average payable period and profitability coefficient of APP is -0.323 and the p value 0.016198 thus shorten the payable period gives good impact on the creditors wont affect the reputation of firm to get the credit .the cash conversion cycle ccc coefficient is -0.349 and the p value is 0.00977 thus the longer or shorten cash conversion cycle significantly affects the profitability.

1.6 CONCLUSION

In financial decision of firm managing working capital is important one, adequate level of working capital is needed to the smooth running of the business. The firms management can lengthen the time period for the average collection period which attracts and sustain the customers raise the profitability. It can also lengthen the inventory conversion period thus raises the profitability. Paying the credits within the time limit helps the strengthen the credit scoring rating so again when the firm is needed of funds it can being get from the creditors. Through the effective and efficient utilization of resources reducing cash conversion cycle speed up the profitability of the firm. Thus working capital management deals with cash accounts receivable and inventories raise the profitability of the firm.

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