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Efficiency of Working Capital Management with Reference to Select Textile Industry in India

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Abstract

Financial efficiency is desirable in all organization as an individual mission. It measures the intensity with which a business uses its assets to generate gross revenue and the effectiveness of producing, purchasing, pricing, financing, and marketing decisions. The aim on the paper to study the growth and development of Indian Textile industry. To analyze the trends and patterns of efficiency of Working capital utilization of selected Textile companies in India. For the purpose have selected 20 companies in textile sector and analyze with the help of ratio techniques and simple statistical tools. The study has concluded strongly from the analysis of the data that profitability in terms of profit margin is significantly and affected by the decline in days in accounts receivable, days in accounts payable and Cash conversion cycle in textile firms. It is found that working capital variables have considerable impact on return on assets of textile firms.

Key words: Financial Efficiency, Profitability, Textile Industry, Utilization Index, Working Capital Index.

I. INTRODUCTION

The Indian Textile Industry is a vertically integrated industry which covers a large gamut of activities ranging from production of its own raw material namely, cotton, jute, silk and wool to provide the consumers high value added products such as fabrics and garments. To sustain this growth, it is imperative that the textiles industry must produces goods of high quality at reasonable price and moderating its machinery. Therefore, the textile machinery industry sector has an integral role to play in the growth of Indian export industry. The textile products are increasing worldwide as more and more in developing countries enter into global textile trade. In order to maintain its global market share, the Indian textile industry must procure modern, low-cost, textile machinery so that it can produce high quality of textile products and garments for export at competitive price.

II. THEORETICAL BACKGROUND

A. *Financial Efficiency*

Financial efficiency is a measure of an organizations ability to translate its financial resources into mission related activities. Financial efficiency is desirable in all organization as an individual mission. It measures the intensity with which a business uses its assets to generate gross revenue and the effectiveness of producing, purchasing, pricing, financing, and marketing decisions. At the micro level financial efficiency refers to the efficiency with which resources are correctly allocated among competing uses at a point of time. Financial efficiency is a measure of how effectively an organization has managed certain risk and return, liquidity and profitability in the use of its financial resource. Financial efficiency is regarded as a measure of total efficiency and the extent of the profitability, liquidity, productivity and capital strength can be taken as a final proof of a financial efficiency.

B. *Measurement Tools of Financial Efficiency*

Financial efficiency is a measure of an organizations ability to translate its financial resources into mission related activities. Financial efficiency is desirable in all organization as an individual mission. It measures the intensity with which a business uses its assets to generate gross revenue and the effectiveness of producing, purchasing, pricing, financing, and marketing decisions. At the micro level financial efficiency refers to the efficiency with which resources are correctly allocated among competing uses at a point of time. Financial efficiency is a measure of how effectively an organization has managed certain risk and return, liquidity and profitability in the use of its financial resource. Financial efficiency is regarded as a measure of total efficiency and the extent of the profitability, liquidity, productivity and capital strength can be taken as a final proof of a financial efficiency.

III. REVIEW OF LITERATURE

Ghosh and Maji (2004) conducted the efficiency of working capital practices in Indian cement industry had been examined by using some alternate measures of working capital management. Three measures, performance index of working capital, utilization index of working capital and efficiency index of working capital were used to measure the overall efficiency of Indian cement manufacturing firms. The data about 20 large cement industries were collected for 10 years from 1992-2001. The results indicated that Indian cement industry did not perform remarkably well during the study period in terms of working capital management. Industry average for efficiency index of working capital was greater than 1 for only 6 years out of 10 years of study. However, some of the sample firms improved their efficiency index during the study period but a high degree of inconsistency was found into working capital management practices.

Arindham Ghosh (2007) in his article attempted to study the impact of working capital ratios on profitability viewed both positive and negative impacts. Out of the nine ratios selected for the study, three ratios namely current assets to sales ratio, working capital turnover ratio and debtors' turnover ratio showed a negative correlation with the ROI. The rest namely working capital ratio, acid test ratio, current assets to total assets, inventory turnover ratio, cash turnover ratio and miscellaneous current assets turnover ratio showed positive correlation. The study of the relationship between the profitability and working capital ratio confirm with accepted rule that larger the turnover, more the profitability of the company.

Farhan Shehzad et.al. (2012) examined the working capital management efficiency of the textile companies of Pakistan for the period of 2004 to 2009. Three index variables that were performance index, utilization index and efficiency index were constructed along with Financial Debt Ratio (FDR) and Fixed Financial Asset Ratio (FFAR) which acts as control variables for measuring the efficiency of working capital management. To apprise the relations among WCM Efficiency and EBIT in selected firms of Pakistan's Textile industry regression analysis was used. FDR and FFAR which acts as control variables were also used for measuring the efficiency of WCM. These control variables showed significant and negative relation with EBIT. Regression results also show the significant relationship of WCM efficiency and earnings before interest and tax. PI, UI & EI showed the positive relationship among EBIT its mean if the company manage WC efficiently it might lead towards increase the earnings/ income. FDR & FFAR ratio showed negative relation with EBIT and company/ firm could increase earnings through reducing the debt and fixed financial resources.

Talat Afza and Mian Sajid Nazir (2011) conducted a careful investigation since the working capital management played an important role for the firm's profitability and risk as well as its value. It required continuous management to maintain proper level in various components of working capital i.e. cash, receivables, inventory and payables etc. The present study was an attempt to evaluate the efficiency of the working capital management of cement sector of Pakistan for the period 1988-2008. Using industry norm as target efficiency level of the individual firms, an evaluation had been made with regards to the speed of achieving that target level of efficiency by an individual firm during the study period. It observed that overall efficiency of cement sector with respect to working capital management had remained satisfactory as index value of EIWCM was greater than 1 in 18 out of 20 years of the study.

Debdas Rakshid and Chanchal Chatterjee (2012) their study observed that working capital management practice of four selected Indian Pharmaceutical Companies. For this purpose the working capital utilization index had been used and the appropriate rise in sales was more than the proportionate increase in current assets over a particular period of time. The study revealed that angle of overall efficiency in WCM, Novartis India and Abbott India had registered satisfactory performance over the study period. The result of Efficiency Index values showed that wide fluctuation and more than unity value only for four years and also proved that improper utilisation of the current assets.

Asha Sharma (2013) his study examined that impact on liquidity as well profitability. The impact on effectiveness and profitability of working capital was tried to find out by measuring the fluctuation in fixed assets, current assets and sales. For this purpose conducted five years data from 2008 to 2012 of two major companies in public and private sector of steel industry like Steel Authority of India and Tata Steel Ltd., was undertaken. SAIL and TCS had perfect correlation between its fixed and current ratio and as well they had a perfect correlation with its liquidity and profitability. Keeping in view the miniature amount of finance literature, particularly in profitability, liquidity and working capital, the present study investigates the relationship of the aggressive and conservative financial performance analysis and financial polices and how its impact on profitability. It further examines that efficiency of working capital utilization among the working capital practices of the firms across the different industries.

IV. NEED FOR THE STUDY

The Indian textile sector is growing at a rapid pace and is getting international recognition. It is also taking adequate measures for the development of export oriented products, attracting new investments both domestic and foreign. Besides this sector has significant importance of employment generation, industrial, social and economical in nature. Working capital is an important part of finance having a vital bearing on the liquidity of a company. Hence, in this study focuses on facts on working capital management analysis are made on clear understanding of financial performance of the selected companies and also predict to determine the overall financial position of the industry. This study would help the shareholder the investors, policymakers, managers, researchers and people who are involved in financial decision.

V. STATEMENT OF PROBLEM

Textile Industry is providing one of the most basic needs of people and to maintain sustained growth for improving standard of life. It has a unique position as a self-reliant industry, from the production of raw materials to the delivery of finished products, with substantial value-addition at each stage of process. It is a major contribution to the country's economy. At present the textile industries are affected by so many problems such as, shortage of power, shortage of working capital, shortage of raw material, obsolete technology under-utilization of capacity, shortage of labour, inability to meet interest commitments, non-payment of loans, non-provision of depreciation , absence of sound infrastructure support, high cost of production, poor profitability and managerial incompetence. These factors ultimately have an adverse impact on profitability. Working Capital Management always affects marketing, production, personal and other areas of management. For the success of every business concern not only fair capitalization is required, but the management of working capital is very much important for its concern and its profitable operations. The overall financial performance is an important factor which indicates the growth of any industry that comprises liquidity, profitability and working capital.

VI. OBJECTIVE OF THE STUDY

- To study the growth and development of Indian Textile industry.
- To analyze the trends and patterns of efficiency of Working capital utilization of selected Textile companies in India.
- To suggest measures for effective operations and offer recommendations for the improvement of efficiency in Textile industry.

VII. METHODOLOGY

Research is a process of a systematic and in-depth study or search of any particular topic, subject or area of investigation, backed by the collection, compilation, presentation and interpretation of relevant details or data. It is a careful search or inquiry into any subject or subject matter, which is an endeavour to discover or find out valuable facts, which would be useful for further application or utilization researchers and analysis of management problems would result in certain conclusions by means of logical analysis. A scientific approach to the research methodology is very much essential to evaluate the research problem systematically.

A. Framework of Analysis

For the purpose of analyzing working capital management of the study makes use of various accounting ratios extensively. Ratio analysis helps in comparison of performance of different companies and, summary of various statistical techniques, such as mean and utilization index have been used for analyzing and interpreting the secondary data.

B. Data Collection

In the present study an extensive use of secondary data which are not gathered specially to meet the needs of the problem at hand. For this study, data have been collected for the period of fifteen years from 1997 to 2011.The published annual reports from CMIE PROWESS database and other publications such as stock exchange official directory, Economics times, Financial Express, RBI Bulletin and Other periodicals Journals have also been used

C. Sample Size

There are 750 Textile companies listed at CMIE Database out of which 20 are selected on the basis of Net Asset Value exceeds Rs. 1000 Crores. The firms are not included as sample whose data is not available or observations are missing for few years. The data used for the research consist of annual data for the period of fifteen years. The annual data under the study period is used as the variables in the research.

D. Period of the Study

The study covers a period of fifteen years from 1997 to 2011 and an accounting year of the company consisting of 12 months from 1st April to 31st March.

E. Limitation of the study

This study is based on secondary data derived from published annual reports of the selected Textile companies. The reliability and findings are largely depending on the published data in the annual reports. The different views have been applied in the calculation of different ratios. The present study is largely based on ratio analysis. It has its own limitations. The study restricted to selected 20 companies in Textile Industry.

VIII. DATA ANALYSIS AND INTERPRETATION

For examining the efficiency in utilization of Working Capital three different indices, viz., Performance Index (PI), Utilization Index (UI) and Efficiency Index (EI) are calculated. If cost and current assets of the business have moved with the sales index to generate profits, an index can be worked out by comparing cost with sales. It is necessary to develop such indices that are expected to capture the operational efficiency of a firm.

Table 1.1
Working Capital Performance Indices of Textile Industry
(Based on Summary of Mean Value during 1998-2011)

Name of the Company	**Utilization Index**	**Performance Index**	**Efficiency Index**
KSL Industries Limited	1.52	5.27	6.64
JCT Limited	1.06	1.08	1.05
RSWM Ltd	1.01	1.39	1.44
Nagar Limited	1.09	2.01	2.46
Century Limited	1.03	1.21	1.27

Nagar Spinning Mills	1.01	1.35	1.41
Garden Silk Limited	0.99	1.44	1.46
JBF Industries Limited	1.01	2.01	2.29
Trident Limited	1.05	2.03	2.23
WELSPUN India Ltd	1.03	1.70	1.76
SRF Limited	1.00	1.75	1.80
Bombay Dying Co. Ltd	1.15	1.48	1.70
SKumars nationwide	1.05	1.66	1.76
Raymond Ltd	1.03	1.13	1.17
Indo Rama Ltd	1.02	1.30	1.40
Vardhmann Textiles Ltd	1.02	1.59	1.68
Arvind Textiles	0.99	1.28	1.21
Alok Industries	1.04	2.29	2.47
National Textiles	0.97	0.96	0.91
Grasim Industries	1.01	1.13	1.14

Source: Computed

In Table 1.1 portrays that comparative analysis of working capital indices. The Average Utilization Index of selected companies under study is more than unity value. In Aravind Mills Ltd and Garden Silk Ltd has the utilization Index which was below the unity value and the National Textiles Ltd has the highest value depicted during the study period. The overall study period wise analysis reveals that utilization index is poor during the year 1999, 2003, 2004, 2005 and 2009. The Average Performance Index of selected companies under study is more than unity value. Among the selected companies National Textiles Ltd and KSL has the highest value of performance index under the study. The overall study period wise analysis reveals that performance index is poor during the year 2001, 2003 and 2009. Efficiency index is a product of performance and utilization index and it measures the efficiency of Working Capital Management. The JCT Ltd, Raymond Ltd, Arvind Mills Ltd and Century Textile Ltd have shown the poor efficiency index compared with other companies. The National Textiles Corporation and KSL Ltd have the high efficiency index and shown better performance of working capital management. The overall study period wise analysis reveals that efficiency index is poor during the years 1999, 2003, 2004, 2005 and 2009.

IX. CONCLUSION

The study has analyzed the working capital efficient relationship of textile industry in India. It is found from the analysis of the data that profitability in terms of profit margin is significantly and affected by the decline in days in accounts receivable, days in accounts payable and Cash conversion cycle in textile firms. It is found that working capital variables have considerable impact on return on assets of textile firms. It can be concluded that the company's overall risk evaluation process is not at desired level and should be concentrate on liquidity and working capital management and it should be managed effectively and reviewed periodically and thereby optimum utilization of fixed assets is possible. It is further concluded that can be strengthened if firm is managed its working capital management through effective ways.

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