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A Study On Working Capital Management At Aravind Mills

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Abstract-The fixed and the current assets play a vital role in the success of any company. Managing the working capital is mandatory because, it has a huge significance on profitability and liquidity of the business concern. The increase in working capital helps in improving its liquidity. Thus, a company needs to have a correct balance between the liquidity position and the profits of the company. The various components for measuring the working capital management include the receivable days, Inventory turnover ratio, Payable days, Cash conversion cycle, Current ratio and Quick ratio on the Net operating profitability position of the Indian companies. The various factors like fixed assets on total assets, the Debt ratio and the size of the firm have also been used for measuring of the working capital management.

Keywords: Profitability, Liquidity, Current ratio and Quick ratio, Working Capital

INTRODUCTION

The primary objective of any firm is to maximize their profits. But, maintaining the liquidity of the firm is also an essential objective. The problem is that growing profits at the cost of liquidity can bring major and effective problems to the firm. Therefore, there must be a proper balance between these two objectives or goals of the firms. One objective should not be met at cost of the other. If we do not care about profit, it becomes difficult to survive for a longer period. On the contrary if we do not care about liquidity, we may have to face the problem of insolvency or bankruptcy. For the above reasons management of working capital should be given proper importance and as it ultimately affect the profitability of the firm. Hence firms have to maintain an optimal level of working capital

CONCEPT OF WORKING CAPITAL USED

- **Gross Working Capital Concept**
- **Net Working Capital Concept**

GROSS WORKING CAPITALCONCEPT:-

According to the gross concept, working capital means total of all the current assets of a business. Where current liabilities are not deducted from current assets to find the working capital. It is also called as Gross Working Capital.

NET WORKING CAPITALCONCEPT:-

According to the net working capitalconcept, net working capital means the excess of current assets over current liabilities. According to this concept, if current assets are equal to current liabilities, working capital will be zero and in case current liabilities are more than current assets, the working capital will be negative.

Current assets are those, which are converted into cash within the accounting year. For instance, Stock, Debtors, Bills Receivables, cash and bank balanceetc. Similarly, current liabilities are those liabilities which have to be paid withinthe accounting year, for instance, Creditors, Bills Payable, Short-Term Loans Etc.

Net working capital can also be defined in another fashion. Net working capital is that part of current assets which have been financed from long-range funds. It is, hence called circulating capital or fixed working capital.

Gross concept and net concept of working capital have their own significance. When one current asset is to be managed, gross concept of working capital is used. Net concept of working capital stresses on how much current assets have to be financed out of long-term funds

NEED FOR WORKING CAPITAL:-

For the various operations of the business, working capital is required along with the fixed capital. Working capital is needed for the buying of material and payment of various day to day expenses. There is no business which does not require working capital. The requirement for working capital is different in different businesses. Financial management looks up to maximizing the wealth of shareholders. To achieve this objective, it is necessary to earn adequate profits. The profits depend hugely on sales but sales do not result in cash immediately. To increase sales, goods are to be sold on credit basis, the collection of which takes place after a period of time. Thus there exists a gap between sale of goods and collection of cash. During such period expenses are to be incurred to continue business operations for this concern working capital is required. In addition the smooth conduct of business operations, maintenance of fixed assets, payment of petty expenses, and payment of debts on maturity, building of reputation of business largely depends upon the efficient management of working capital.

It can be depicted with the help of operating cycle:**-**

The larger the period of operating cycle, more will be the requirement of working capital. Business enterprise

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involved in trading activities have lesser duration of operating cycle as compared to those engaged in manufacturing business , as in such enterprise cash is directly converted into finished goods.

COMPONENTS OF WORKING CAPITAL MANAGEMENT:-

The three fundamental components of working capital management. They are:-

INVENTORY MANAGEMENT:-

Inventory management is the process of efficiently checking the constant flow of inventory components into and out of an existing inventory. This process involves controlling the transfer in of inventory components in order to prevent the inventory from becoming too high, or decreasing to danger level that could put the operation of the company into jeopardy. Competent inventory management also aims at controlling heavy investment of capital, the costs related to the inventory, both from the perspective of the total value of theinventory componentsincluded and the tax payments generated by the cumulative value of the inventory.

CASH MANAGEMENT:-

The comprehensive process of collecting, managing and (short-term) investing cash. A key element of ensuring company's financial firmness and solvency. Often corporate treasurers or a business manager is responsible for total cash management.

A good cash management involves not only avoiding liquidationbut also dropping days in account receivables (AR), increasing collection rates, selecting suitable short-term investment vehicles, and rising days cash on hand all in order to improve a company's overall financial profitability.

RECEIVABLES MANAGEMENT:-

The credit and the collection efforts should be laid down properly and effectively implemented to manage the accounts receivables systematically. The credit policies should be such that balance the risk on one hand and profitability on the other hand. The venture in the receivables should be at the optimum level.

ESTIMATION OF WORKING CAPITAL:-

TECHNIQUES:-

There are certain methods used for finding the optimum level of working capital or management of different items of working capital.

- **Intersection of Carrying Cost and Shortage Cost:** One of the important methods of finding the optimum level of working capital is the point of meeting of carrying cost and Storage cost in a graphical representation. The total of carrying and Storage cost is at the least point.

Here, the levels of current assets are optimum at the point where the Storage and carrying costs are intersecting. At this point, the total cost, as we can see, is minimum and this is why that level of current assets is regarded to be optimal.

- **Working Capital Financing Policy:** Working capital can be divided into two types. Permanent and Temporary. Permanent working capital is the level of working capital which is always required. Temporary working capital is the part of working capital which keeps on fluctuating. It is more in good seasons and less in bad seasons. There are two types of financing available. They are long and short range financing. Three strategies are possible with respect to financing of working capital. Efficient financing of working capital decreases carrying cost of capital.

  Long term financing is used for permanent as well as temporary WC.

  Long term financing is used for permanent and some regions of temporary WC. Left over part of temporary WC is financed through short term financing as and when required.

  Long range financing is used for permanent and short range financing for temporary WC.

  These strategies should be chosen so as to match the source of finance with the maturity of the asset.

- **Cash Budgeting:** Cash budgeting is another mainmethod for working capital management which helps keeping optimum level of cash in the business. Cash budgeting includes estimating the needs of cash by estimating all the fore coming receipts and payments. For efficient management, a balance is required between both excess and shortage of cash. It is because both ends are costly. Fastening up of collection and getting calm credit terms from the creditors can reduce the cash requirements.

- **EOQ**: Economic Order Quantity (EOQ) model is a famous model for managing the inventories. It helps the inventory manager know how to find the right quantity that should be ordered considering other factors like cost of ordering, carrying costs, purchase price and annual sales. The formula used for finding EOQ is as follows:
- Just-in-Time: Just-in-time is another important method which brought about paradigm shift in the management of inventories. It did not decrease the cost of inventory but it abolished it completely. Just-in-time means acquiring material or product at the time when it is required by the customer. This strategy is hard to put into operation but if practiced can bring down inventory cost to minimum.

These are some important techniques discussed here. They are very effective in controlling working capital. Working capital means managing current assets. Current assets like cash can be controlled using cash budgeting; inventory can be controlled by using inventory techniques like EOQ and JIT. Debtors and financing of working capital can be controlled by using appropriate sources of finance.

Need for the Study

Today financial reliability and productivity of business enterprises largely depend upon the working capital management by the firm. If there is inadequacy of working capital it affects the day to day operations of the business firm, if there is surplus of working capital, fund become idle it also affects the financial soundness of the firm. In this point of view there is need to control the working capital effectively in any business. The question which strike the mind during reviewing different literatures that how KPCL managing its working capital being public sector undertaking. Hence study is conducted to answer the above stated question.

Objectives of the Study

- ✓ To learn the sources and uses of the working capital.
- ✓ To study the liquidity position through various working capital related ratios.
- ✓ To suggest based on the findings of the study.

Research Methodology

Research is the step by step process of collecting and analyzing data for the purpose of increasing our understanding of the phenomenon about which we are interested. It is the in detail search for knowledge. It is a careful investigation or inquiry especially through search for fresh facts in any branch of knowledge. The study exhibits both descriptive and analytical character. With respect to the theoretical concept it is descriptive since it interprets and analysis the secondary data in order to reach atsuitable conclusion, it is also analytical in character. The interpretation of data is done based on ratios and proportions.

Research Design

Research Design is the strategy for the study and the plan by which the strategy is to be carried on. It is the set of judgment that make up the master plan specifying the methods and procedures for the collection, dimension and analysis of data. Research has used descriptive research. Descriptive studies are fact finding investigation with appropriate interpretation. It aims on particular aspects of in the study. It is designed to gather detail information and provides information for formulating more sophisticated studies

Data collection:

- The secondary data used is collected from the articles on WCM published in magazines and from the various papers onAravind Mills.

Here we done the analysis on basis of secondary data, which included-

- Balance sheet of Aravind Mills
- Profit and loss A/C of Aravind Mills
- Cost sheets, & Trail balance of Two years

DATA ANALYSIS AND INTERPRETATION

It would look as a practical solution to this crisis to keep a very high balance in the cash and marketable securities account. In this path, when flow hindrances occur, hasty and painful remedial actions will not be necessary since the huge reserves provides some safety; the leaks can be plugged before the water is exhausted. However, such a strategy can depress the degree of a firm's productivity, since cash and marketable securities are two of the firm's least profitable assets. A main function of decision making for working capital is the management of the various working capital assets with respect to the firm's level of liquidity: not too much liquidity and not too little liquidity.

WORKING CAPITAL ANALYSIS:-

As we are aware that working capital is the support and the centre of a business. Adequate amount of working capital is very importantfor the smooth functioning of the business. And the most important part is the efficient management of working capital in right time. The liquidity status of the firm is totally effected by the management of working capital. So, a study of variations in the uses and sources of working capital is necessary to evaluate the efficiency with which the working capital is utilized in a business. This includes the need of working capital analysis.

KEY WORKING CAPITAL RATIO ANALYSIS:

A ratio is a simple arithmetical expression of one number to another. The technique of ratio analysis can be employed for measuring short-term liquidity or working capital position of a firm. The following ratios can be calculated for these purposes:

1. Current ratio.
2. Quick ratio
3. Absolute liquid ratio
4. Inventory turnover Ratio.
5. Receivables turnover.
6. Working capital turnover ratio

Ratios	Formula	2015	2014	2013	2012	2011
Current Ratio	$\frac{Current\ Assets}{Current\ liabilities}$	.83:1	.85:1	.75:1	.67:1	.76:1
Quick Ratio	$\frac{Quick\ Assets}{Quick\ Liabilities}$	1.56: 1	1.59: 1	1.34: 1	1.11: 1	1.35: 1
Absolute liquid Ratio	$\frac{Absolute\ Quick\ Assets}{Current\ Liabilities}$	.017: 1	.057: 1	.074: 1	.021: 1	.017: 1
Inventory Turnover Ratio	$\frac{\text{Cost of Goods Sold}}{\text{Average Stock}}$	5.02	5.07	4.32	4.80	3.84
Receivables Turnover Ratio	$\frac{\text{Net Credit Annual Sale}}{\text{Average Trade Debtor}}$	10.65	9.93	8.92	7.21	5.43
Working Capital Turnover Ratio	$\frac{\text{Cost of Sales}}{\text{Average Working Capi}}$	77.11	17.64	6.89	15.75	45.70

CURRENT RATIO:

A current ratio of 2:1 is considered as ideal: if a business has an undertaking with its bankers to meet its working capital requirements at short notices, a current ratio of is adequate. A relatively high current ratio is a indication that the firm is liquid and has the ability to pay its current obligations in time as and when they become due. On the other hand, a relatively high current ratio represents that the liquidity position of the firm is not good and the firm shall not be able to pay its current liabilities in time without facing difficulties.

Arvind Paper Mills hada current ratio of 0.76 in the year 2011and 0.67 in the year 2012 was decreasing trendand it was 0.75 in the year 2013 which was increasing trend and it was 0.85 in the year 2014 and it was 0.83 in the year 2015 which was a slight decrease when compared to previous year.However the company needs to work on increasing its current ratio as this ratio symbolizes the financial health of an organization

QUICK RATIO:

A Quick ratio of 1:1 is considered as ideal: if a business has an undertaking that which can meet its current financial obligations with the available quick funds on hand. A high quick ratio is an indication that the firm is liquid and has the ability to meet its current or liquid liabilities in time on the other hand a low quick ratio represents that the firm's liquidity position is not good.

Arvind paper mills had a quick ratio of 1.35 in the year 2011and1.11 in the year 2012 and it was 1.34in the year 2013 and it was1.59 in the year 2014 and it was1.56 in the year 2015.Based on this interpretation we can say that Quick ratio is more satisfactory. It may therefore be said that short term liquidity of the company is very sound.

ABSOLUTE LIQUID RATIO:

A absolute liquid ratio 0.5:1 is considered as ideal. This ratio is useful only when used in conjunction with current ratio and quick ratio. The acceptable norm for this ratio is 50% or 1:2 that is Rs. 1 worth absolute liquid assets are considered adequate to pay Rs. 2 worth current liabilities in time as all the creditors are not expected to demand cash at the same time and then cash may also be realized from debtors and inventories.

Arvind paper mills had absolute liquid ratio of .017 in the year 2011and .021 in the year 2012 and it was .074in the year 2013 and it was.057 in the year 2014 and it was 0.17 in the year 2015.The trend is not depicting a positive sign, hence the company should take measures to bring its absolute liquid ratio to the required standards which will be of great help to the company.

INVENTORY TURNOVER RATIO:

It is also knows as stock velocity.An Inventory turnover ratio indicates the number of times the stock has been turn over during the period and evaluates the efficiency with which a firm is able to manage its inventory. A high inventory turnover indicates efficient management of inventory because more frequently the stocks are sold, the lesser amount of money is required to finance the inventory. A lower inventory turnover indicates a inefficient management of inventory.

Arvind paper mills had Inventory turnover ratio of 3.84 in the year 2011and 4.80in the year 2012 and it was 4.32in the year 2013 and it was5.07 in the year 2014 and it was 5.02 in the year 2015.The stock velocity ratio of Arvind mills depicts an increasing trend, which a good sign which shows that the velocity of stock getting converted to cash is in a good pace.

RECEIVABLES TURNOVER RATIO

A Receivable turnoverratioindicates the relationship between net credit sales and trade debtors. It shows the rate at which cash is generated by the turnover of debtors. Debtors turnover indicates the number of times there debtors are turned over during the year. Generally, the higher the value of debtor's turnover the more efficient is the management of debtors/sales or more liquid are the debtors. Similarly, low debtors turnover implies inefficient management of debtors/sale and less liquid debtors.

Arvind paper mills had Inventory turnover ratio of 5.43 in the year 2011and 7.21in the year 2012 and it was 8.92in the year 2013 and it was9.93 in the year 2014 and it was 10.65 in the year 2015.It shows that year by year its recovery rate is increasing.There is an increasing trend in the receivables turnover ratio, which shows that there is a good collection efforts by the company and they are using good collection techniques which may require less investment in working capital, it may also show that there are more of cash sales and less on credit basis.

WORKING CAPITAL TURNOVER RATIO

A working capital turnover ratioindicates the velocity of the utilization of net working capital. This ratio indicates the number of times the working capital is turned over in the course of a year. This ratio measures the efficiency with which the working capital is being used by a firm. A higher ratio indicates the efficient utilization of working capital and a lower ratio indicates otherwise.

Arvind Paper Mills had a working capital ratio of 45.70 in the year 2011and 15.75 in the year 2012 was decreasing trend and it was 6.89 in the year 2013 which was increasing trend and it was 17.64 in the year 2014 and it was 77.11 in the year 2015.

There exists a lot of fluctuations in the working capital turnover ratio, the company must take steps to efficiently utilize the available resources and allocate the same and also control the requirement which will reduce the cost to the company.

FINDINGS AND SUGGESSIONS

FINDINGS:

- ✓ Working capital of Arvind mills was increasing and showing positive working capital per year.
- ✓ The Arvind mill has a higher quick ratio. So the company's liquidity position is good. It shows that it is able to meet its current obligation.
- ✓ Receivable turnover ratio depicts an increasing trend.so the cash position of the company is good.
- ✓ Quick ratio is also higher than the standard of 1:1, which shows that the company has good liquid position.
- ✓ Current ratio trend shows that the ratio is above the required standards of 2:1. Based on this data, liquid position of the company shall be considered as satisfactory.

SUGGESTIONS

- ✓ Working capital of the company is decreasing few years. The company has to take care of the decreasing trend in the long run as it will affect the company.
- ✓ The quick ratios are almost up to the standard requirement. So the working capital management of Arvind Mills is satisfactory and it as to maintain it further.
- ✓ Current ratios is also up to the standard expected, hence Aravind Mills is position is satisfactory.
- ✓ The cash position of the company is good, and hence it symbolizes that, there is prompt collection efforts.

CONCLUSION

By concluding the study about the working capital it is found that working capital management of Aravindmills is too good. Aravind Exports has sufficient funds to meet its current obligation every time which is due to sufficient profits and efficient management of Aravind Exports.

Cash management and receivable management are too much good because of centralized control on these. Raw material for the all units of Aravind Exports is purchased by corporate office in bulk which is the best way. Safety methods for inventories are also quiet sufficient in company. Hence it reduces the idle time of the workers, requires less supervision on employees as there will be continuous supply of materials and hence full capacity of plant is utilized .Overall the working capital management of Aravind Mills is very much efficient.

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