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Impact of Working Capital Management on Financial Performance & Share Price: Evidence from Indian FMCG Companies

Dr. Sanjeeb Kumar Dey

P.G. Department of Commerce, Ravenshaw University,
Cuttack, Odisha, 753003, India

Abstract

Working capital constitutes that portion of funds that facilitates the normal day to day activities of the organisation. No doubt a strong fixed capital base is essential for survival and growth of firm, but adequate working capital ensure the smooth functioning of operation. Working capital affects both short-term and long-term financial position of the business. The present paper is an attempt to study the impact of working capital management on the profitability of the firms through ratio analysis. The profitability of the firms has been measured in terms of net profit margin, return on net worth and earnings per share. The secondary data has been collected from various websites and the study covers a period of five years i.e. 2011-2015. The analysis has been conducted on five top Fast Moving Consumer Goods Companies operating in India. The results show that there is short-term financial scarcity in almost all the five companies. Our study also revealed that besides ITC, all other companies have a negative or low amount of working capital and they rely more on their creditors for their sale growth. HUL is most vendor dependent company. The working capital management is not satisfactory in any companies except ITC.

Keywords: *Working capital management, FMCG companies, Profitability, Share Price*

1. Introduction:

Working capital means the flow of funds crucial for the working of an undertaking. It constitutes funds invested in Current Assets, which can be converted into cash within a short period without changing the value and without agitating the functioning of the organization. Aside from investing in fixed assets, it is also imperative for every business to have enough funds to meet the day-to-day expenses. Current assets are indispensable to use fixed assets profitably. Be it any form of business or any type of environment, working capital is inevitable for a business to survive and grow.

The FMCG sector is one of the most vibrant sectors in India. The Indian FMCG industry is the 4th largest sector in India with an estimated market size of 2 trillion. In the last decade, the FMCG sector has grown at an average of 11% a year; in the last five years, annual growth accelerated at a compounded rate of 17.3%. Indian FMCG companies have a competitive advantage due to availability of key raw materials, cheaper labor costs and presence across the entire value chain.

2. Review of Literature:

S.C. Mohanty (2014) has studied the effectiveness of Working Capital Management in selected organizations along with its needs and efficiency. He concluded that there is a difference in liquidity management between the public and private companies, no association between current ratio and profitability for a few sample companies and inventory or debtors' turnover found to be not associated with profitability for a few sample companies.

B Bagchi & B Khamrui (2012) have studied the relationship between working capital management and firm profitability and to identify the variables that most affect profitability. They found that there is a strong negative relationship between variables of the working capital management and profitability of the firm.

Mosa Ahmadi, et. el. (2012) found that the relationship between the working capital components and profitability is negative. This means the increase in receivable days, payable days; inventory days and cash conversion cycle can decrease the profitability of the company. They suggest that in order to maximize the wealth of the shareholders managers needs to focus on the

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effective management of working capital components.

Bhaskar Bagchi, et. el. (2012) studied the impact of working capital management on corporate profitability of Indian FMCG firms. They found that there is a sturdy negative association between working capital management variables and firms' profitability.

3. Objectives of the study:

- . To study the financial performance of sample companies considering few selected performance ratios.
- To assess the impact of working capital management on financial performance and share price of the sample companies

4. Methodology of the study:

The present paper is an ex-post facto research study. It is basically based on secondary sources of data collected from moneycontrol.com. The study covers top five FMCG companies i.e. HUL, ITC, Britannia, Nestle and Marico operating in India and covers five years i.e. 2011-2015. For analysis of data, statistical measures like Arithmetic Mean, Coefficient of Variation (CV), etc. are used with the help of software like Minitab and Microsoft Excel 2010.

5. Results and Discussion:

Current ratio is an important indicator of sound working capital of the firm. It establishes the relation between current assets and current liabilities. Normally 2:1 is considered as standard ratio and sound position. It does not necessarily mean that firm not having standard ratio is unsound in working capital management. It simply shows how much current assets are funded by short term credit and borrowing. Table no. 1 depicts, none of the companies under study, have achieved the standard rule of thumb of the current ratio i.e. 2:1. Both year-wise and company-wise average current ratio of all the companies' ranges from 0.50 to 1.70. Marico has the highest average current ratio i.e. 1.70 while the average of all the companies is highest in the year 2015 i.e. 1.13. The degree of variedness is highest in 2015 which is 44.61%. Among the companies there is highest variation in case of Britannia i.e. 14.65%. The analysis indicates that there is short-term financial scarcity in almost all the five companies.

Quick ratio indicates the liquidity position further only considering quick assets as compared to current liabilities and 1:1 is considered as standard position Analysis of quick ratio in table no 2 reveals that the average quick ratio of not a single company is up to the standard which is 1:1 except Marico

Table No. 1 – Analysis of Current Ratio

Company	Mar-15	Mar-14	Mar-13	Mar-12	Mar-11	Average	CV
HUL	0.75	0.74	0.76	0.83	0.86	0.79	6.08
ITC	1.45	1.25	1.22	1.12	1.09	1.23	10.35
Nestle	0.53	0.65	0.54	0.55	0.62	0.58	8.29
Britannia	1	0.84	0.79	0.7	1.04	0.87	14.65
Marico	1.94	1.32	1.69	1.72	1.83	1.70	12.32
Average	1.13	0.96	1.00	0.98	1.09		
CV	44.61	28.44	40.93	41.97	37.31		

(Source: www.moneycontrol.com)

. The average quick ratio ranges from 0.50 to 1.20 both ways. Quick ratio is highest in Marico i.e. 1.20 and lowest in Nestle i.e. 0.28. The average quick ratio is highest in the year 2011 i.e. 0.67. While variation is not so significant in the companies with highest variation of only 25.59% in Marico but there is significant variance among the period of study with a highest of 69.55% in 2012. The analysis of quick ratio implies that except Marico, no company has the ability to meet its current liabilities.

Table No. 2 – Analysis of Quick Ratio

Company	Mar-15	Mar-14	Mar-13	Mar-12	Mar-11	Average	CV
HUL	0.47	0.44	0.45	0.46	0.46	0.46	2.24
ITC	0.87	0.68	0.66	0.56	0.53	0.66	18.11
Nestle	0.25	0.39	0.22	0.27	0.27	0.28	20.70
Britannia	0.7	0.47	0.58	0.36	0.52	0.53	21.50
Marico	0.87	0.81	1.27	1.47	1.56	1.20	25.59
Average	0.63	0.56	0.64	0.62	0.67		
CV	38.11	28.71	55.07	69.55	68.22		

(Source: www.moneycontrol.com)

The analysis of inventory turnover ratio in table no 3 depicts that average inventory turnover ratio is highest in Britannia i.e. 16.44. The table shows that Britannia Company has been able to sell its inventories better than the other companies. The inventories of all the companies were turned for the highest times in the year 2015 i.e. 11 times. Variation is also highest in case of Britannia i.e.

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17.66% and there is high variance in the year 2015 i.e. 47.81%.

Table No. 3 – Analysis of Inventory Turnover Ratio

Company	Mar-15	Mar-14	Mar-13	Mar-12	Mar-11	Average	CV
HUL	12.57	10.76	10.8	9.21	7.34	10.14	17.33
ITC	6.43	4.52	4.53	4.47	5.85	5.16	15.91
Nestle	11.67	12.37	11.55	10.49	12.33	11.68	5.85
Britannia	21.24	17.19	16.94	13.17	13.68	16.44	17.66
Marico	5.92	5.55	4.81	5.61	5.18	5.41	7.07
Average	11.57	10.08	9.73	8.59	8.88		
CV	47.81	46.05	47.72	37.12	39.09		

(Source: www.moneycontrol.com)

Table 4 shows that average debtors' turnover ratio is highest in Nestle i.e. 95.57 but variation is highest in HUL i.e. 16.19%. The average debtors' turnover ratio is highest in the year 2015 i.e. 62.69 which means 2015 was the most successful year in collecting the receivables. It is clear from the analysis that Nestle is the most successful company in collecting its receivables frequently. Variation is highest in HUL i.e.16.19% and highest in the year 2011 i.e. 66.36%.

Table No. 4 – Analysis of Debtors Turnover Ratio

Company	Mar-15	Mar-14	Mar-13	Mar-12	Mar-11	Average	CV
HUL	38.52	33.96	34.13	27.27	24.34	31.64	16.19
ITC	18.78	19.97	27.82	26.91	24.61	23.62	15.41
Nestle	107.49	105.92	82.12	84.1	98.22	95.57	11.16
Britannia	115.12	96.44	86.89	90.94	87.31	95.34	10.98
Marico	33.56	27.05	30.3	27	22.02	27.99	13.73
Average	62.69	56.67	52.25	51.24	51.30		
CV	64.27	64.82	50.63	57.95	66.36		

(Source: www.moneycontrol.com)

Table 5 reveals that the average working turnover ratio is the highest in Britannia i.e. 298.26 and the lowest in HUL i.e. -14.95. It indicates that, on an average, Britannia Company is efficient in using its short-term assets and liabilities to support sales whereas HUL is borrowing more& more credit from its vendors to support its sales. The average working capital turnover ratio is highest in the year 2015 i.e. 310.81 and lowest in the year 2013 i.e. -43.34. The coefficient of variance analysis shows that there is highest variance in the ratios of Britannia i.e. 215.87% and lowest& negative variance in HUL i.e. -21.19%.

Table No. 5 – Analysis of Working Capital Turnover Ratio

Company	Mar-15	Mar-14	Mar-13	Mar-12	Mar-11	Average	CV
HUL	-13.14	-11.55	-12.6	-17.99	-19.49	-14.95	-21.19
ITC	8.29	10.45	11.51	21.36	38.11	17.94	61.51
Nestle	-7.16	-9.51	-8.09	-9.2	-9.72	-8.74	-11.08
Britannia	1559.4	-39.97	-211.51	-14.82	198.22	298.26	215.87
Marico	6.68	7.1	4.01	4.08	3.59	5.09	29.14
Average	310.81	-8.70	-43.34	-3.31	42.14		
CV	200.87	-205.90	-195.04	-436.42	190.87		

(Source: www.moneycontrol.com and calculated in MS Excel)

Table 6 depicts that average net profit margin of ITC is the highest i.e. 25.05 and the lowest in Britannia i.e. 5.18. It means ITC has been efficient in managing the affairs if the business. The average net profit margin is highest in the year 2014 i.e. 14.80 and lowest in the year 2012 i.e. 12.90. The analysis also reveals that there is highest variation in the ratios of Britannia i.e. 37.42% and lowest variation in Nestle i.e. 3.07%. 2012 has the highest variation of 51.49% and the working capital turnover ratio is the lowest in 2015 i.e. 42.21%.

Table No. 6 – Analysis of Net Profit Margin

Company	Mar-15	Mar-14	Mar-13	Mar-12	Mar-11	Average	CV
HUL	14	13.8	14.7	12.16	11.68	13.27	8.67
ITC	26.31	26.43	24.8	24.47	23.24	25.05	4.78
Nestle	12.02	12.27	12.81	12.79	13.07	12.59	3.07
Britannia	8.67	5.86	4.16	3.75	3.44	5.18	37.42
Marico	11.64	15.67	12.59	11.33	13.41	12.93	12.02
Average	14.52	14.80	13.81	12.90	12.96		
CV	42.21	45.14	47.72	51.49	48.55		

(Source: www.moneycontrol.com)

The analysis in table 7 shows that the average return on net worth is highest in HUL i.e. 107.85% and lowest in Marico i.e. 28.02%. It means that shareholders of HUL are receiving almost 100% return on their investment for the last five years whereas the shareholders of Marico are getting the lowest returns among the five companies under study. There is highest variation in the ratios of case of Nestle i.e. 30.80% and lowest variation in case of ITC which is 2.96%. The average return on net worth ratio is highest in the year 2013 i.e. 58.61% and lowest in the year 2015 i.e. 46.51%. The able also depicts that there is highest variation in the ratios in 2015 i.e. 76.25% and lowest in 2012 i.e. 42.30%.

Table No. 7 – Analysis of Return on Net Worth

Company	**Mar -15**	**Mar -14**	**Mar -13**	**Mar -12**	**Mar -11**	Average	CV
HUL	115.87	118.04	142.01	76.62	86.72	107.85	21.77
ITC	31.31	33.51	33.36	32.88	31.36	32.48	2.96
Nestle	41.75	47.16	59.38	75.47	95.7	63.89	30.80
Britannia	20.37	43.33	36.74	35.9	32.19	33.70	22.47
Marico	23.26	29.25	21.54	29.94	36.11	28.02	18.56
Average	46.51	54.26	58.61	50.16	56.42		
CV	76.25	59.97	74.17	42.30	50.69		

(Source: www.moneycontrol.com)

The average earning per share, as depicted in table 8, is highest in Nestle i.e. 106.83 which also has the lowest variation of 12.46%. It is clear that per share earnings of the investors is the highest in Nestle among the five companies under study. The average earning per share is highest in 2015 i.e. 43.03 and lowest in the year 2011 i.e. 23.87. The table also depicts that there is highest variation in the ratios of Britannia i.e. 55.28%. The ratios have lowest variation in 2015 i.e. 99.38% and highest in 2011 i.e. 128.35%.

Table No. 8 – Analysis of Earnings Per Share

Company	**Mar -15**	**Mar -14**	**Mar -13**	**Mar -12**	**Mar -11**	**Average**	**CV**
HUL	19.95	17.88	17.56	12.45	10.68	15.70	22.43
ITC	11.99	11.05	9.39	7.88	6.45	9.35	21.62
Nestle	122.87	115.87	110.76	99.73	84.91	106.83	12.46
Britannia	51.9	30.84	19.57	15.63	12.16	26.02	55.28
Marico	8.45	8.95	6.65	5.47	5.13	6.93	22.21
Average	43.03	36.92	32.79	28.23	23.87		
CV	99.38	108.92	119.83	127.24	128.35		

(Source: www.moneycontrol.com)

Table 9 shows that share price of Nestle has the highest average of Rs. 4982.78 and Marico has the lowest average i.e. Rs. 111.54. There is highest variance in the ratios of Britannia i.e. 71.95% and lowest in Nestle i.e. 21.68%. It is also observed from the table that the highest average share price is Rs. 2100.89 i.e. in 2015 and the lowest average share price is Rs. 921.30 i.e. in 2011. There is highest variation in the year 2011 i.e. 151.20% and lowest in 2015 i.e. 120.26%.

Table No. 9 – Analysis of Share Price

Company	**Mar -15**	**Mar -14**	**Mar -13**	**Mar -12**	**Mar -11**	Average	CV
HUL	873	603.65	465.2	412.3	284.1	527.65	38.05
ITC	326.9	352.5	309	226.85	182.35	279.52	22.99
Nestle	6961	5030.05	4620	4602.85	3700	4982.78	21.68
Britannia	2150	845	525	592.5	370.55	896.61	71.95
Marico	193.53	104.8	105.4	84.5	69.5	111.54	38.67
Average	2100.89	1387.20	1204.92	1183.80	921.30		
CV	120.26	132.51	142.23	145.13	151.20		

(Source: www.moneycontrol.com)

Figure 1 shows the relationship between working capital, net profit & share price of HUL. It is seen that working capital goes on decreasing with a negative trend but Net Profit & Share Price have increased over the years. It shows a direct inverse relationship between working capital and net profit & share price. The net profit and share price seem to be unaffected with the decrease in working capital even in negative figures.

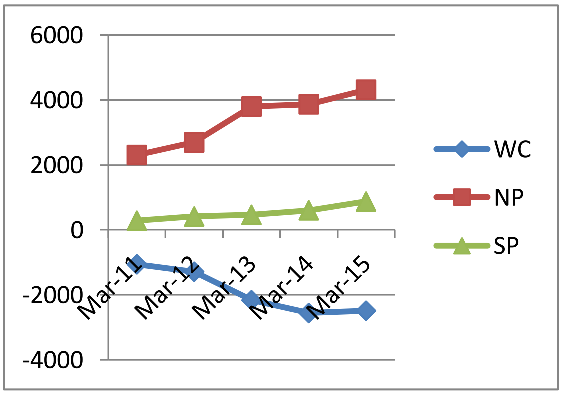

Figure 1: Relationship between Working Capital, Net Profit & Share Price of HUL

Figure 2 depicts the relationship between working capital, net profit and share price of Britannia. It is observed from the figure that working capital is fluctuating over the period of study but net profit & share price are increasing. It is seen that net profit is affected to some extent by working capital but share price have a negative relationship with working capital.

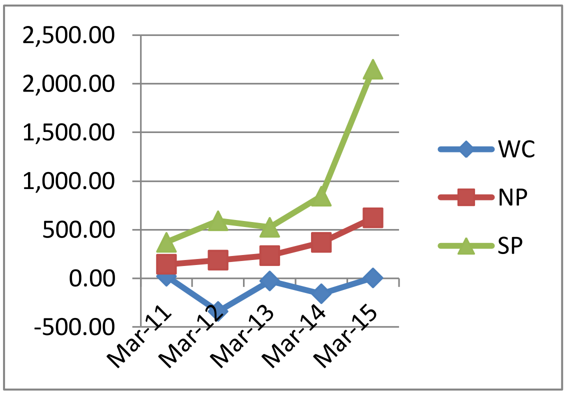

Figure 2: Relationship between Working Capital, Net Profit & Share Price of Britannia

Figure 3 shows the relationship between working capital, net profit and share price of ITC. It is seen from the figure that both working capital and net profit have an increasing trend while there is not much change in the share price of the company. Net profit seems to be positively affected by working capital but it does not have a significant impact on the share price.

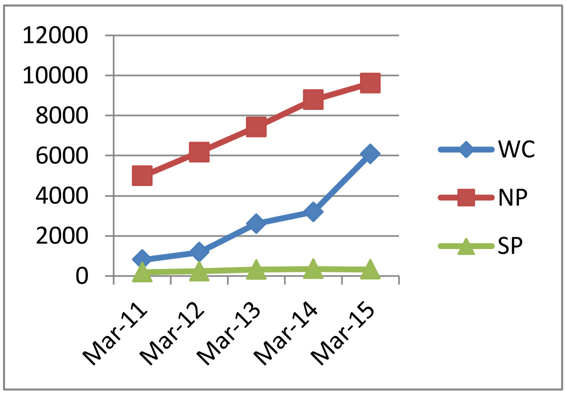

Figure 3: Relationship between Working Capital, Net Profit & Share Price of ITC

Figure 4 illustrates the relationship between working capital, net profit and share price of Marico. It is noticed from the figure that working capital, net profit &share price are having almost a rising trend and share price is not much influenced by working capital. Net profit seems to be less influenced by working capital during the period of study.

The relationship between working capital, net profit and share price of Nestle is shown in figure 5. It is observed from the figure that both net profit and share price have a direct negative relationship with working capital because as working capital goes on decreasing, net profit & share price goes on increasing in an increasing manner. It is found from the figure that working capital has no impact on net profit & share price.

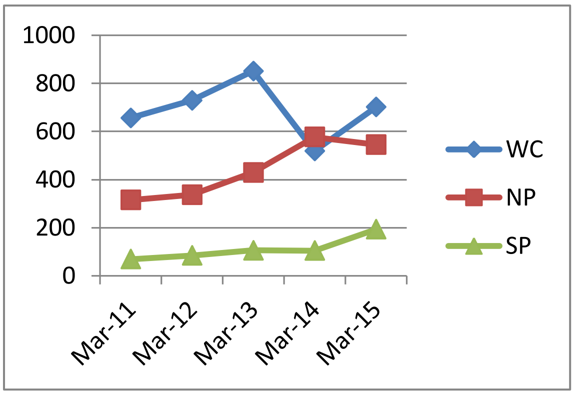

Figure 4: Relationship between Working Capital, Net Profit & Share Price of Marico

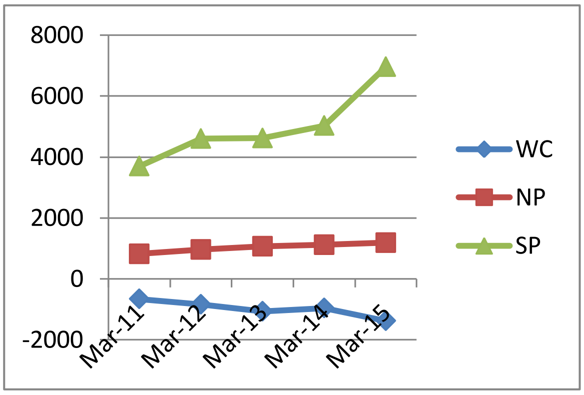

Figure 5: Relationship between Working Capital, Net Profit & Share Price of Nestle

6. Conclusion:

Most of the companies are using high credit from suppliers and financing most of the current assets from current liabilities which is not good sign of liquidity position of the firms. In spite of the fact, companies could able to earn more return on net worth and margin over the years. This may be possible because of strategic management current assets and liabilities which is not possible throughout the year. It is also evident from the study that there is negative relationship between working capital management measures and profitability and share price of the companies. It can be concluded that the companies should try to improve their working capital position to avoid sudden liquidity crisis. The result could be more accurate and generalized if more number of companies and long period would be taken into account.

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