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Review Of Research

"AN ANALYSIS OF THE WORKING CAPITAL MANAGEMENT - A MACRO LEVEL INVESTIGATION IN HUBLI ELECTRICITY SUPPLY COMPANY"

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ABSTRACT

Management of the working capital is nothing but the management of current assets and it is the nerve system of any business. Without proper working capital management a company cannot achieve its objectives and it is not possible to come out from weak financial conditions. So in this perspective the present study on working capital management at Hubli Electricity Supply Company is conducted through macro level investigation or ratio analysis and some statistical tools (CAGR and AGR) and charts are also adopted. The present work has used secondary sources like Annual reports, Economic surveys and working papers which are published by Govt. of Karnataka.

KEYWORDS: Working capital management, Current ratio, Quick ratio, HESCOM.

I. INTRODUCTION

Working capital may be regarded as the life blood of the business enterprise. It is very closely relating to the day to day operations of the business. Any business we consider requires two types of funds, namely the long term and short term fund. The long term is required for creation of production facilities such as plant and machineries, land and buildings, furniture's and fixtures etc. The fund invested in current assets such as stock of material, work-in-process, bills receivables, sundry debtors etc. is known as working capital.

The term working capital refers to that part of total capital which is required for financing the current or working need of the business enterprise. It is the finance required for day to day working in a business concern, such as the amount invested in inventories, bills receivables, etc. Working capital is also known as circulating capital. And it is also known as short term capital. Because as compared to fixed capital it is invested generally for short period. Apart from this the concern requires a certain amounts for its day to day functioning such an amount is called short term fund.

Hubli Electricity Supply Company Limited is one of the biggest power distribution companies in Karnataka, serving seven of its districts. It was formed in the year 2002 under the Companies Act. HESCOM has the sole responsibility for power distribution in Dharwad, Gadag, Bijapur, Bagalkot, Uttara Kannada, Haveri and Belgaum districts of Karnataka.

Present work has been undertaken at Hubli Electricity Supply Company. The research dealt with “An analysis of the working capital management - A macro level Investigation in Hubli Electricity Supply Company”. In this study an attempt has been made to understand the Working Capital Management of the organization and try to give solution to solve the problems and to achieve objectives of the company.

II.GENERAL DEFINITION OF WORKING CAPITAL

Working capital refers to that part of firm’s capital which is required for Financing short term or current assets such as cash, debtors, inventories and marketable securities.

The term working capital refers to-

a) Those current assets which are convertible into cash within the period of one Accounting year and
b) Those funds which are needed for meeting day to day operations.

III.Components of Working Capital
There are two components of Working Capital
A.Current Assets
B.Current Liabilities

A) Current Assets:

Components of Current Assets are as follows:

1. Cash & Bank Balance
2. Stock of Raw Material at cost- work in process and Finished Goods.
3. Advanced Recoverable in Cash or kind or kind or for value to be received.
4. Deposits under the company scheme.
5. Advanced payment of income takes credit certificates..
6. Outstanding debts for a period exceeding six months.
7. Balance with central excise authorities.

B) Current Liabilities:

Components of Current Liabilities are as follows:

1. Sundry Creditors for the goods and expenses.
2. Income tax deducted at sources from contractors.
3. Expenses Payable.
4. Unclaimed Dividend.
5. Security Deposits.
6. Liabilities for bills discounted.
7. Bank Overdraft Acceptance.

IV. DETERMINANTS OF WORKING CAPITAL:

The following is the description of factors which generally influence the working capital requirements of HESCOM –

1 Nature of Business: This is one of the primary factors influencing the working capital requirements of a firm. The Company is a manufacturing firm, has a longer operating cycle for manufacturing the products, and investing more funds in its current assets. Therefore, it requires much more working capital.

2. Manufacturing Cycle: It comprises of the purchase and use of raw materials and the production of finished goods. Longer the manufacturing cycle, large will be the firm's working capital requirements.

3. Credit Policy: The credit policy relating to sales and purchases also affects the working capital. The credit policy influences the requirement of working capital in two ways:

iCredit terms generated by the firm to its customers.
iiCredit terms available to the firm from its creditors.

4. Growth & Expansion: As a firm grows, it is logical to expect that a large amount of working capital is required. The growth in volume of the business effects the requirements of working capital. If the firm goes on diversifying its activities, the working capital is also increases.

5. Price Level Changes: Changes in the price level also affect the requirements of working capital. The rising price levels will require a firm to maintain higher amount of working capital. Same level of current assets will need increased investment when price are increasing.

6.Operating Efficiency & Performance: The operating efficiency of the firm relates to the optimum utilization of resources at minimum costs. The firm will be effectively contributing to its working capital if it is efficient in controlling operating costs. The use of working capital is improved and pace of cash cycle is accelerated with operating efficiency.

7. Level of Taxes: Tax liability is the short-term liability day able in cash. The amount of taxes to be paid in advance creates the need for working capital. If the tax liability increases, it leads to an increase in the requirement of working capital and vice versa. The need for working capital varies with the tax rates and advance tax provisions.

8. Sales Growth: The working capital needs of the firm increase as it sales grow. The growing firm may need to invest funds in fixed assets in order to sustain its growing production and sales. This will in turn, increase investment in current assets to support enlarged scale of operations.

V. OBJECTIVES OF THE STUDY

1. To understand the concept of working capital and its importance
2. To analyze the working capital management financial performance of the HESCOM
3. To offer suggestions based on findings of the study

VI. SCOPE OF THE STUDY

The present study is restricted to Hubli Electricity Supply Company.

VII. DATA COLLECTION

To achieve the above mentioned objectives, data is gathered from secondary sources like annual reports, journals, and related other research papers.

VIII. DATA ANALYSIS

The collected data is analysed through ratio analysis. Growth rates and important tables are used for data discussion as per the research need.

IX. ANALYSIS AND INTERPRETATION

Management of the working capital is nothing but the management of current assets. The management of the current assets includes Inventory, Received, Debtors, Book debts, Short-term assets cash and bank balances. Working Capital refers to the amount of capital which is readily available to an organization that is, working capital is the difference between resources in cash and readily convertible into cash (current assets) and organizational commitments for which cash will soon be required (current liabilities).

The present study is regarding the working capital and its management of the Hubli Electricity Supply Company Limited (HESCOM). Therefore, the research is restricted only to the working capital management. The data information is collected from annual reports from 2002-03 to 2011-12

Gross working capital consists of all the current assets held by the company. The list of various current assets held by the firm is given below.

Table no.1
Structure of current assets in (crore)

SL. No	Particulars/ Years	2002-2003	2003-2004	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	2011-2012
1	Inventories, stores and spares	51.77	45.4	16.35	20.31	21.56	33.15	37.29	34.41	34.85	66.3
2	Sundry debtors	427.4	312.5	497.77	669.34	813.24	1062.4	1206	1364.6	1565.6	1524.96
3	Cash and bank balance	25.66	32.22	18.57	34.43	27.44	446.71	84	32.39	33.36	146.12
4	Loans and advances	12.6	13.2	25.82	70.07	161.42	219.32	64	63.73	76.24	686.15
5	Other assets	19.52	537.17	767.37	672.12	644.46	157.12	560.02	900	991.58	519.08
Total current assets		**536.95**	**940.49**	**1325.9**	**1466.27**	**1668.1**	**1918.7**	**1951.3**	**2395.2**	**2701.6**	**2942.6**

Source: Annual reports 2002-03 to 2011-12

The table given above, depicts the current assets of the company from 2002-03 to 2011-12. During 2002-03 total currents assets was Rs. 536.95 crores , in the year 2007-08 Rs. 1918.7 crores, in the year 2009-2010 Rs. 2395 crores, and in the 2011-2012 Rs.2942.6 crores. From the above table it can be observed that there is a tremendous increase in the value of current assets from the year 2002-03 to 2011-12, which indicates extensive growth of the organization. But during 2002-03 to 2010-11 inventory assets is declining continuously.

Table no .2

				Structure of current liabilities					in (crore)		
SL. No	Particulars/ Years	2002-2003	2003-2004	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	2011-2012
1	Power of Purchase Liabilities	178.85	485.01	742.46	576.61	917.54	460.05	875.53	1171.2	1586.2	1649.4
2	Liabilities for inter Company Transactions	181.58	329.48	258.03	237.95	180.97	460.37	469.03	427.89	433.66	137.19
3	Staff related Liabilities	12.66	3.89	6.4	13.69	17.53	138.08	160.92	66.47	97.87	66.47
4	Other Liabilities	26.96	53.23	61.02	88.91	37.45	22.11	45.61	156.32	168.85	754.68
Total Current Liabilities		**400.05**	**871.61**	**1067.9**	**917.16**	**1153.5**	**1080.6**	**1551.1**	**1821.9**	**2286.6**	**2607.8**

Source: Annual reports 2002-03 to 2011-12

The above table depicts the current liabilities of the company from 2002-03 to 2011-12. During 2002-03 total currents assets was Rs. 400.05 crores , in the year 2007-08 Rs. 1080.6 crores, in the year 2009-2010 Rs. 1821.9 crores, and in the 2011-2012 Rs.2607.8 crores. From the above table it can be observed that there is a tremendous increase in the value of current liabilities from year 2002-03 to 2011-12.

Table no.3

				Working Capital					in Crore		
SL. No	Particulars/ Years	2002-2003	2003-2004	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	2011-2012
1	Total Assets (A)	536.95	940.49	1325.9	1466.27	1668.1	1918.7	1951.3	2395.2	2701.6	2942.6
2	Total Liabilities (B)	400.05	871.61	1067.9	917.16	1153.5	1080.6	1551.1	1821.9	2286.6	2607.8
Total Working Capital (A-B)		**136.9**	**68.88**	**257.97**	**549.11**	**514.63**	**838.09**	**400.22**	**573.25**	**414.99**	**334.86**

Source: Annual reports 2002-03 to 2011-12

Net working capital is the resultant of excess of current assets over current liabilities, so the list of current liabilities up to the year 2011-12 is given. The table given above shows the total working capital from the year 2002-03 to 2011-12.

The previous statement shows that company had invested in its current assets and incurred liabilities. Therefore the company’s Net Working Capital requirement in these all years (i.e. A-B) is Net Working Capital requirement.

ANALYSIS

a. Current ratio: This ratio is an indicator of firm’s commitment to meet its short term liabilities. Higher ratio indicates the better solvency conditions; 2:1 ratio is treated as standard ratio. It is the ratio of current assets and current liabilities. To find out the current ratio the following equation is used.

$$Current\ Ratio = \frac{Current\ Assets}{Current\ Liabilities}$$

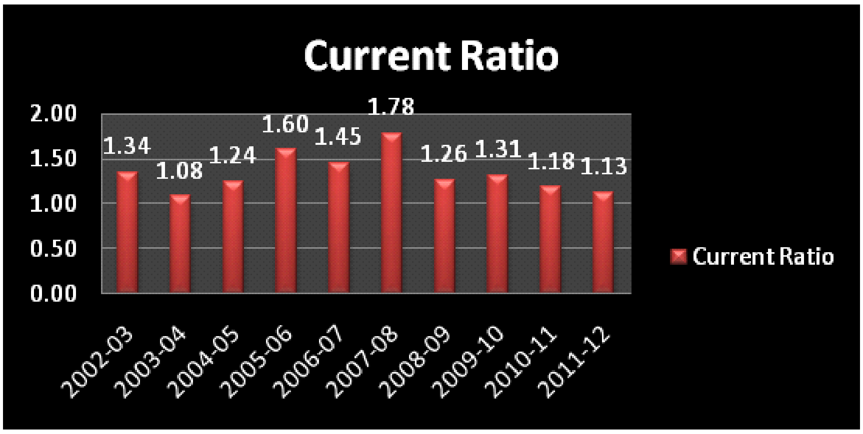
Table no.4

Structure of Current Ratio				
SL.No	**Year**	**Current Assets**	**Current Liabilities**	**Current Ratio**
1	2002-03	536.95	400.05	1.34
2	2003-04	940.49	871.61	1.08
3	2004-05	1325.9	1067.91	1.24
4	2005-06	1466.3	917.16	1.60
5	2006-07	1668.1	1153.49	1.45
6	2007-08	1918.7	1080.61	1.78
7	2008-09	1951.3	1551.09	1.26
8	2009-10	2395.2	1821.91	1.31
9	2010-11	2701.6	2286.6	1.18
10	2011-12	2942.6	2607.75	1.13

Source: Annual reports 2002-03 to 2011-12

The current ratio for ten years from 2002-03 to 2011-12 are calculated and presented in the above table. From the above table it is analyzed that the current ratio position in the company is not good and it shows that the company had less than 2 current ratio, which is considered as insufficient liquidity and the firm’s liquidity of the years 2003-04 and 2011-12 is very less, it’s about near to 1, which clearly indicates the lower rate of liquidity.

Figure no .1



Source: Annual reports 2002-03 to 2011-12

The figure given above shows the structure of current ratio form 2002-03 to 2011-12, it can be observed in the above figure that the company’s current ratio is less than 2. Except 2005-06 and 2007-08 in these two years the current ratio is almost near to two.

From this we can understand that the company had held current assets to meet its currents liabilities.

Table no.5

Working Capital Growth rates				
Years	**Assets**	**Liabilities**	**Working Capital**	**AGR**
2002-03	536.95	400.05	136.9	
2003-04	940.49	871.61	68.88	-31.12
2004-05	1325.9	1067.91	257.97	157.97
2005-06	1466.3	917.16	549.11	449.11
2006-07	1668.1	1153.49	514.63	414.63
2007-08	1918.7	1080.61	838.09	738.09
2008-09	1951.3	1551.09	400.22	300.22
2009-10	2395.2	1821.91	573.25	473.25
2010-11	2701.6	2286.6	414.99	314.99
2011-12	2942.6	2607.75	334.86	234.86
CAGR	**18.54**	**20.61**	**9.35**	

Source: Annual reports 2002-03 to 2011-12

From the table given above it is analyzed that the working capital compound annual growth rate of the company is 9.35 in the period 2002-03 to 2011-2012, and total assets CAGR is 18.54 and total liabilities CAGR is 20.61, the table indicates the total liabilities excess total assets it is not good for company's economic condition and annual growth rate is fluctuating year on year. In the year 2003-04 it was negative (about -31.12) and the year 2007-08 recorded highest growth rate which was 738.09. This shows that the company's liquidity position is unstable.

b. Quick ratio: Liquid ratio is indicated of quick assets to honour its immediate claim, higher the ratio better the coverage and standard ratio is 1:1 as asset is liquid it can be converted into cash immediately in the value of profit and loss.

Table no. 6

Structure of Quick Assets									in (crore)		
SL. No	**Particulars/ Years**	**2002-2003**	**2003-2004**	**2004-2005**	**2005-2006**	**2006-2007**	**2007-2008**	**2008-2009**	**2009-2010**	**2010-2011**	**2011-2012**
1	Sundry debtors	427.4	312.5	497.77	669.34	813.24	1062.4	1206	1364.63	1565.56	1524.96
2	Cash and bank blance	25.66	32.22	18.57	34.43	27.44	446.71	84	32.39	33.36	146.12
3	Loans and advances	12.6	13.2	25.82	70.07	161.42	219.32	64	63.73	76.24	686.15
4	Other assets	19.52	537.17	767.37	672.12	644.46	157.12	560.02	900	991.58	519.08
Total Quick assets		**485.18**	**895.09**	**1309.53**	**1445.96**	**1646.56**	**1885.55**	**1914.02**	**2360.75**	**2666.74**	**2876.31**

Source: Annual reports 2002-03 to 2011-12

The above table depicts the quick assets of the company from 2002-03 to 2011-12. During 2002-03 total quick assets was Rs. 485.18 crores, in the year 2007-08 it was Rs. 1885.55 crores, in the year 2009-2010 Rs. 2360.75 crores, and in the 2011-2012 Rs.2876.31 crores. From the above table it can observed that there is a tremendous increase in the value of quick assets from year 2002-03 to 2011-12, which indicates extensive growth of the organization.

Table no. 7

Structure of Quick Liabilities											in (Crore)
SL. No	Particulars/ Years	2002-2003	2003-2004	2004-2005	2005-2006	2006-2007	2007-2008	2008-2009	2009-2010	2010-2011	2011-2012
1	Power of Purchase Liabilities	178.85	485.01	742.46	576.61	917.54	460.05	875.53	1171.2	1586.2	1649.4
2	Liabilities for inter Company Transactions	181.58	329.48	258.03	237.95	180.97	460.37	469.03	427.89	433.66	137.19
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Total Current Liabilities		**400.05**	**871.61**	**1067.9**	**917.16**	**1153.5**	**1080.6**	**1551.1**	**1821.9**	**2286.6**	**2607.8**

Source: Annual reports 2002-03 to 2011-12

The above given table depicts the quick liabilities of the company from 2002-03 to 2011-12. During 2002-03 total quick liabilities was Rs. 400.05 crores, in the year 2007-08 Rs. 1080.6 crores, in the year 2009-2010 Rs. 1821.9 crores, and in the 2011-2012 Rs. 2607.8 crores.

From the above given table it can observed that there is a tremendous increase in the value of current liabilities from year 2002-03 to 2011-12.

The following equation is used for the calculation of quick ratio:

❖ $$quick\ ratio = \frac{current\ assets}{current\ liabilities}$$

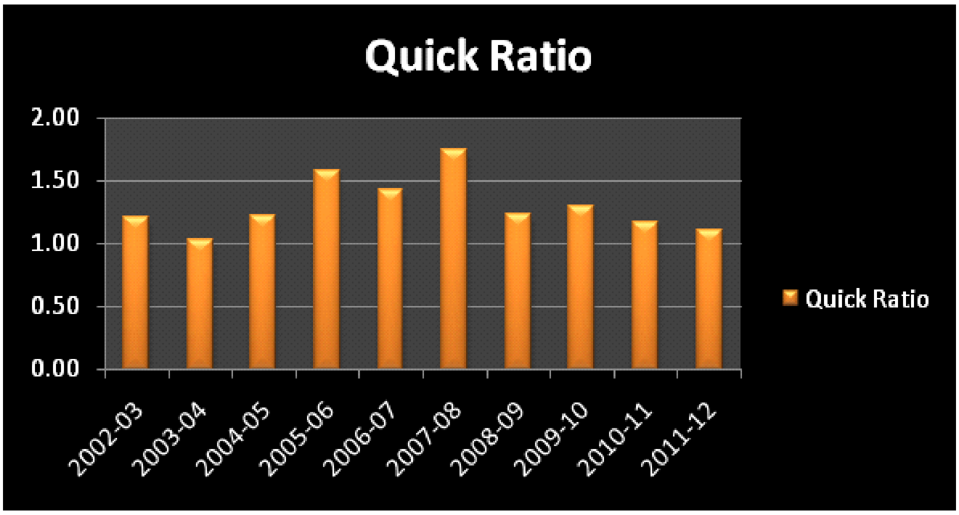
Table no.8

Structure of Quick Ratio				
SL.No	Year	Quick Assets	Quick Liabilities	Quick Ratio
1	2002-03	485.18	400.05	1.21
2	2003-04	895.09	871.61	1.03
3	2004-05	1309.53	1067.91	1.23
4	2005-06	1445.96	917.16	1.58
5	2006-07	1646.56	1153.49	1.43
6	2007-08	1885.55	1080.61	1.74
7	2008-09	1914.02	1551.09	1.23
8	2009-10	2360.75	1821.91	1.30
9	2010-11	2666.74	2286.6	1.17
10	2011-12	2876.31	2607.75	1.10
CAGR		**19.47**	**20.61**	

Source: Annual reports 2002-03 to 2011-12

The above given table analyses that the status of quick assets, quick liabilities and quick ratio, in the duration 2002-03 to 2011-12 the company's quick assets compound annual growth rate is 19.47 and quick liabilities compound annual growth rate is 20.61 and these two rates are almost same, it means quick assets are near to equal quick liabilities and quick ratio for the same period is almost more than one, this shows that the company's liquidity position is good. Generally a Quick Ratio 1 to 1 is considered to represent a satisfactory current financial condition.

Figure no. 2



Source: Annual reports 2002-03 to 2011-12

The above given figure shows the structure of quick ratio form 2002-03 to 2011-12. From the figure 2 we can understand that the company has the good liquidity condition. It shows that the quick ratio is almost more than one in all periods and in 2005-06 and 2007-08 it was more than 1.5, but now it is comparatively coming down.

Generally a Quick Ratio 1 to 1 is considered to represent a satisfactory current financial condition and here which is more the satisfactory level. A Quick Ratio 1 to 1 or more does not necessarily imply sound liquidity position. It should be noted that all the debtors may not be liquid and cash may be immediately needed to pay operating expenses. It should be noted that inventories, are not absolutely non-liquid. Thus company with a high value of Quick Ratio can suffer from the shortage of funds if it has doubtful slow paying and long duration outstanding debtors on the other hand. A company with low value of Quick Ratio may really be prospering and paying its current obligation in time if it has been tarring over its inventories efficiently. Nevertheless, the Quick Ratio remains an important index of a firm's liquidity.

X. FINDINGS:

- Table no.1 indicates that the company's Current assets are moving upwards year by year. From this it can be observed that the Firm is more efficient in its current assets.
- Table no.2 shows that the company's Current liabilities are changing year by year, but the current liabilities are lesser than current assets. It indicates that the firm is efficient in its current liabilities.

- The variations took place in the total net working capital are found from table no. 3.
- Table no.4 shows the current ratios of different years, the highest peak of the current ratio had took place in the year 2007-08.
- Table no. 5 shows that the company's liquidity position is unstable, in the year 2003-04 it was negative (-31.12) and in the year 2007-08 is recorded highest growth rate was 738.09.
- Company's quick ratio is fluctuating (1.03 to 1.74) hence company has to formulate policies in such a way that such fluctuations can be minimised to a greater extent in the upcoming days.

XI. SUGGESTIONS:

- The company should maintain revenue from sale of power to develop its debtor's turnover ratio.
- The company should increase revenue from sale of power to develop its Inventory turnover ratio.
- The management should take effective measures to recover the outstanding of the company.
- The company should maintain in balance between current assets and fixed assets.
- The company should increase the working capital funds to utilize the fixed assets efficiently.
- The company need to invest more in fixed assets to sustain production and sales.

XII.CONCLUSION

From the study it can be concluded that the company's earnings are increasing every year, the company's funds are not properly utilized and cash balance of the company is required to be improved in order to have immediate liquidity position. Therefore HESCOM should try to improve its financial positions in the coming years.

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