A STUDY ON THE EFFECT OF WORKING CAPITAL ON THE PROFITABILITY OF TCS

Author
Dr.K.R.Sivabagyam
Assistant Professor
Department of Commerce

Sri Krishna Arts and Science College
E-mail Id: sivabagyamkr@skasc.ac.in
Phone no: 7871809789

Co - Authors
C.S.K. Soundarya
R. SaiSowmiya
S.Savitha
Alya Parveen M
M.Com students
E-mail Id soundaryacsk19mco043@skasc.ac.in
saisowmiyar19mco037@skasc.ac.in
savithas19mco041@skasc.ac.in
Phone no: 9688831142, 9952142525, 8508196577.

Abstract:

The fixed and the current assets play an essential role in the accomplishment of any company. Organizing the working capital is imperative because, it has a huge consequence on profitability and liquidity of the business concern. The increase in working capital assist in improving its liquidity. Thus, a company require to have a correct balance between the liquidity position and the profits of the company. The various elements for measuring the working capital management comprise of receivable days, Payable days, Current ratio and Quick ratio on the Net operating profitability position of an organization. The various aspect like fixed assets on total assets, the Debt ratio and the size of the firm have also been used for determining the working capital management.

Keywords: Profitability, Liquidity, Current ratio and Quick ratio, Working capital over total assets.

INTRODUCTION

Working capital is an effective tool for the measurement of both a company's efficiency and its short-term financial position. Working capital is calculated by the difference between the current assets and current liabilities. In the field of financial event of companies, management of working capital is a primary factor, which has a direct positive effect on profits as well as liquidity position of the organization. Liquidity position and the profits of the firm are two different dimensions. Optimum level of liquidity confirms a firm to meet their short-term funds requirement and the optimum management of fund flow can be confirmed by a profitable business. Liquidity position shows the ability of firm to meet its short-term obligations. A firm has to aim at improving its liquidity position and profits while conducting its day-to-day business operations. Management of Working Capital holds greater balance of working capital factors like debtors, inventory and payables and the use of cash efficiently for daily business activities.

Maintenance of optimal working capital balance is sustaining minimum working capital and understanding maximum possible returns. There is a better relationship between profits of the firm and firm’s working capital. The capability of the company to earn profit can be considered as the ability of the firm to maximize its profits. Profits can be obtained by deducting expenditure from the revenue. Profits of a firm can be used as a measure of the financial performance of a firm and the profit position is the assurance for a company to remain working continuously in the business. Working capital management helps to make sure that the company has increased its productivity. Working capital management is important because of its substantial effect on profits of a firm and the existence of a firm in the market. The ability of financial managers to manage their receivables, inventories, and payments has a better effect on the stakeholders and on profitability too.

The main objective of any firm is to maximize their profits. But, maintaining the liquidity of the firm is also an important objective. The major problem is that growing profits at the cost of liquidity can bring major and effective problems to the firm. There must be a proper balance between these two objectives of the firms. One impartial should not be met at cost of the other. If we do not care about profit, it becomes difficult to endure for a longer period. On the contrary if we do not care about liquidity, they may have to face the problem of liquidation or bankruptcy. The above reasons the management of working capital should be given proper importance and as it eventually affects the profitability of the firm. Hence firms has to maintain an optimum level of working capital.

The aim of working capital management is to make sure that a firm has an ability to conduct its activities continuously and that it has ability to satisfy the both meeting the short-term fund requirements and arising operational expenditures. The working capital management involves retain inventories, accounts received and paid, and cash.

REVIEW OF LITERATURE

Bhunia and Brahma (2011) conducted a study to examine and evaluate the importance of liquidity management on profitability as a factor responsible for unfortunate financial performance in the private sector steel Industry in India.

Owolabi and Obida (2012) an attempt is made to measures the relationship between liquidity management and corporate profitability using data from selected manufacturing companies quoted on the floor of the Nigerian Stock Exchange. They found that managers can increase profitability by adopting good credit policy, short cash conversion cycle and effective cash flow management procedures.

Seyed Mohammad Alavinasab and Esmail Davoudi (2013) in their study examined the relationship between working capital management and profitability hundred forty-seven companies were selected for the period of 2005-2009. The results of the statistical test of the hypothesis show a negative significant relationship exist between cash conversion cycle and return on assets and cash conversion cycle and return on equity. However, the relationship between current ratio and return on equity is insignificant.

Moses Joshuva Daniel (2013) in order to analyze financial status of TATA Motors Ltd in terms of Profitability, Solvency, Activity and Financial stability various accounting ratios have been used. The company has stable growth and it shows a greater status in all the areas it works. The company has been suggested to reduce the expenditure as it increases every year. Decrease in expenses will increase the profitability.

Dharmaraj and Kathirvel (2013) In India there is a huge scope for automobile companies. They are financially strong and they are growing at the rate of 17 per cent per annum and contributing to the Indian economy reasonably. Finally, the study provides companies with understanding of the activities that would enhance their financial performances.

STATEMENT OF THE PROBLEM

Working capital management of a firm is essential for the following two reasons. An optimal part of the investment is invested in firm's current assets

A. Level of current assets will change quickly with the difference in sales.
B. The working capital management of a firm will have a greater strike on the firm's profitability.

Hence, this study has been accompanying to know effect of the size and rising of working capital and whether such an investment has extended or reduced over a period of time. After calculating the need of current assets, the important task of the financial manager has to choose suitable source of finance in order to fund firm's various current assets which helps in maximization of profits.

OBJECTIVES OF THE STUDY

- To acknowledge and study the relationship between Management of working capital and Profitability of the firm.
- To find out the consequence of different components of working capital on the profits of the firm.
- To make suggestion for improvement for the successful endurance in the competitive world.

RESEARCH METHODOLOGY

This study was accompanying on the financial data of TCS from the year 2016 to 2020.

COLLECTION OF DATA

This study is based on the secondary data collected from TCS's Annual Report, balance sheet, financial ratios. Data is also drowning out from different websites.

DATA PROCESSING

After the collection of data from different sources, the data has been classified into tables and analysis was accompany based on the classified data. An explanation was drawn on the effect of working capital on firm's profitability and analysis of ratios.

STATEMENT OF CHANGES IN WORKING CAPITAL OF TCS LTD

Working Capital ascertain the company's short term liquidity position or its potential to meet short term liabilities. It is entitling as the difference between a company's current assets and current liabilities.

ANALYSIS AND INTERPRETATION

Liquidity test

Liquid or solvency position is an element that signifies the volume to meet the financial requirements as and when needed. The solvency ratios are used to compute the short term solvency position and designate the capability of a firm to meet its fund obligation whenever they become due current liabilities are used as the index of the ratios because they are taken in order to stand for the most emergency debt, that is retiring within one year or specifically in one operating cycle.

Table No.1.

Liquidity Test (in rupees crore)

YEARS	CURRENT ASSETS	CURRENT LIABILITIES	CURRENT RATIO	QUICK RATIO
2020	79,194	24,026	3.30	3.30
2019	79,032	18,896	4.18	4.18
2018	68,222	14,058	4.85	4.85
2017	68,442	10,701	6.40	6.39
2016	53,377	11,309	4.72	4.72

Source: Compiled from moneycontrol.com

The current asset situation of the company is conferring above the table. It was 53,377 in the year 2016, gradually increased to 68,442 in the year 2017 after it was increased into 79,194 and last year 2020.

The liquid assets position was 11,309 in the year 2016 and eventually reduced to 10,701 in the year 2017 and thus there should be a better management of assets by the company but it increases to 24,026 in the year 2020.

The current and quick ratio is 4.72 in the year 2016 and it started fluctuated in upcoming years and it reached 3.30 in the year 2020.

Solvency test

On second thought of searching for the best ratio, Prof. Edward Altman has accepted a new technique that takes into consideration the five key performance ratios combined into a single score called z-score which gives investors a better picture of a firm's financial health. This method uses five ratios to establish both financial problems and operating crisis of the firms. It used multiple lessening weight age analysis used for the different ratios.

Table.no 2

Solvency Test (in Rupees Cr)

YEARS	2020	2019	2018	2017	2016
Working Capital	55,168	55,168	55,168	55,168	55,168
Total Assets	1,04,975	1,04,975	1,04,975	1,04,975	1,04,975
Total Liabilities	1,04,975	1,04,975	1,04,975	1,04,975	1,04,975
Ratio of Working Capital over Total Assets	0.53	0.60	0.59	0.64	0.54

Source: Compiled from moneycontrol.com

From the above data it can be resolved that even the company has not at all reach the financially healthy set at any point of the time under this study. But from the attain level of 0.54 in 2016 it reaches 0.64 in 2017 implicit the recovery from the financial crisis and make use of an effective turn around strategies. In the very next year it was decreased to 0.59 but after that it started gradually increase and but the last year it again went declined 0.53.

FINDINGS AND SUGGESTIONS

On the basis of key discovery from this study it has been perceive that the management of a firm can grow the value for their shareholders by decreasing the credit period permitted. The management can also make returns for their shareholders by adding more inventories to meet a best level. Firms can also hold long to pay their creditors. Firms are efficient of employing feasible competitive advantage by way of effective and efficient usage of the resources of the firm by reducing the cash transfiguration cycle to its minimum. By doing so, the profits of the firms are awaiting to grow over a period of time.

Therefore, it is suggested that the computing of working capital should be done at a best level. This helps the firm to sustain its current assets and liabilities in a better way and so that more returns can be made obtainable to the shareholders.

CONCLUSION

In this study, it is clear that the overall status of the working capital management of TCS is satisfactory, but there is a need for expansion in inventory. From the beginning stage of the company the working capital is not acceptable. But now it has growing trend, a major portion of the current assets are kept in the form of firm’s stock or inventory, on the other hand other current assets are properly employed and maintained.

The firm's liquidity or solvency position mainly depends upon the inventory size sustained but other factors like debtors, advances and loans, cash and bank balances, bills receivables etc. are also accountable. However, through this study it was initiated that there is need for an instant improvement in working capital and inventory. The management of TCS must try to properly use the inventory and try to hold the required inventory, so that liquidity will not intersect.

References

- Kothari,C.R,. "Research Methodology Methods & Techniques", New Age International Publishers, New Delhi, Second Edition, 2008.
- Pandey, I. M, "Financial Management', Vikas Publishing, House Pvt. Ltd, New Delhi. Ninth Edition, 2010.
- Prasanna Chandra, " Financial Management Theory and Practice", Tata McGram Hill Publishing House, New Delhi, Sixth Edition, 2006.
- Sharma R.K. Shasi K. Gupta, "Management Accounting", Kalyani Publishers, Ludhiana, India, 2003.
- Khan.M.Y and Jain P.K, "Financial Management", Text and Problems", Tata McGraw Hill Publishing Company Ltd, New Delhi, Fourth Edition, 2006. Bhunia, A. and Brahma, B. "Impact of Liquidity Management on Profitability", Asian Journal of Business Management, Volume (3) 2, 108-117, 2011.
- Owolabi, Ajao & Obida, "Liquidity Management and Corporate Profitability: Case Study of Selected Manufacturing Companies Listed on The Nigerian Stock Exchange" Business Management Dynamics, Volume.2, No.2 , pp.10-25, August 2012.
- Seyed Mohammad Alavinasab and Esmail Davoudi, "Studying the relationship between working capital management and profitability of listed companies in Tehran stock exchange", Business Management Dynamics, Volume.2, No.7, pp.01-08, January 2013.
- Dharmaraj, A. and Kathirvel, N, "Analysing the Financial Performance of Selected Indian Automobile Companies". Global Research Analysis, Volume: 2, Issue 4, Pp 18-20, April 2013.
- Moses Joshuva Daniel, A, "A Study on Financial Status of Tata Motors Ltd", Indian Journal of Applied Research, Volume 3, Issue 4, ISSN - 2249-555X, pp.320-322, April 2013.

Websites

- www.moneycontrol.com
- www.indiainfoline.com
- www.tcs.com