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CONTENTS

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   INTRODUCTION

   REVIEW OF LITERATURE

   NEED/IMPORTANCE OF THE STUDY

   STATEMENT OF THE PROBLEM

   OBJECTIVES

   HYPOTHESES

   RESEARCH METHODOLOGY

   RESULTS & DISCUSSION

   FINDINGS

   RECOMMENDATIONS/SUGGESTIONS

   CONCLUSIONS

   SCOPE FOR FURTHER RESEARCH

   ACKNOWLEDGMENTS

   REFERENCES

   APPENDIX/ANNEXURE

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BOOKS

- Bowersox, Donald J., Closs, David J., (1996), "Logistical Management." Tata McGraw, Hill, New Delhi.
- Hunker, H.L. and A.J. Wright (1963), "Factors of Industrial Location in Ohio" Ohio State University, Nigeria.

CONTRIBUTIONS TO BOOKS

- Sharma T., Kwatra, G. (2008) Effectiveness of Social Advertising: A Study of Selected Campaigns, Corporate Social Responsibility, Edited by David Crowther & Nicholas Capaldi, Ashgate Research Companion to Corporate Social Responsibility, Chapter 15, pp 287-303.

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- Schemenner, R.W., Huber, J.C. and Cook, R.L. (1987), "Geographic Differences and the Location of New Manufacturing Facilities," Journal of Urban Economics, Vol. 21, No. 1, pp. 83-104.

CONFERENCE PAPERS

- Garg, Sambhav (2011): "Business Ethics" Paper presented at the Annual International Conference for the All India Management Association, New Delhi, India, 19–22 June.

UNPUBLISHED DISSERTATIONS AND THESES

- Kumar S. (2011): "Customer Value: A Comparative Study of Rural and Urban Customers," Thesis, Kurukshetra University, Kurukshetra.

ONLINE RESOURCES

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WEBSITES

- Garg, Bhavet (2011): Towards a New Natural Gas Policy, Political Weekly, Viewed on January 01, 2012 http://epw.in/user/viewabstract.jsp

NEGATIVE WORKING CAPITAL AND PROFITABILITY: AN EMPIRICAL ANALYSIS OF INDIAN CEMENT COMPANIES

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ABSTRACT

Though there are too many researches has been conducted on the topic working capital management and its impact on profitability, but there is no major research has been done for the negative working capital and its impact on profitability. All the studies on working capital generally states that for the improvement in profitability we should manage our working capital effectively and most of the studies recommended to have good amount of working capital in the organization. All the researches on this topic conclude that the companies should avoid under-investment in working capital if they want higher profit margins. With this paper we made an attempt to study the profitability of organizations which generally operates with low or in the negative working capital zone and tried to find out whether it has any negative impact on the profitability or not. With negative working capital there can be a danger of insolvency but it is not true forever. If the company is having a good image in the market and good relation with their creditors it can get the benefit from the negative working capital also. The present study is an analysis of five top Indian cement companies' working capital and their profitability structure over a period of ten years. The result shows that though there is a positive relationship between working capital and profitability, yet it does not hold good for all the cases and that too always. We have seen companies generating good profit with a negative working capital as well as companies not able to generate good profit even with having good amount of positive working capital. However, it can be said that negative working capital indicates non-liquidity or less liquidity within the firm which is not desirable at each and every stages of business.

KEYWORDS

Working Capital, Cement Companies, Profitability, Liquidity.

INTRODUCTION

Working Capital Management is concerned with the management of the Current Assets and Current Liabilities and the interrelation that exists between them, so to minimize the risk of insolvency and to maximize the return on assets. The ultimate objective of working capital management is to ensure that a firm is able to continue its operations and that it has sufficient ability to satisfy both maturing short term debt and upcoming operational expenses. Working capital management calls for addressing two basic issues how much of current assets an organization should hold and how to finance the investment in them. In the present scenario some companies are using negative working capital and getting a good amount of profits and good return on capital also. Earlier negative working capital is considered as a risk of insolvency of the organizations but at present negative working capital is a sign of managerial efficiency in a business. Earlier it was considered that the companies should avoid under-investment in working capital if they wanted higher profits margins.

Negative working capital is a reverse situation as compared to normal working capital. It is a situation in which current assets are lower as compared to current liabilities. A negative working capital is an indication of managerial efficiency in a business with low inventory and account receivables. This happens because customer pays in advance and so quickly, the business enjoys cash transactions; products are delivered and sold to the customer before the company even pays their suppliers and creditors. Negative Working capital doesn't always mean bad financial condition; it indicates that most of the day to day activities are funded by customers rather than company's own working capital. Some latest examples are movie theaters - customers are paying first and distributors are normally paid later on; Schools/ educational institutions- fees paid in advance by the students annually, whereas faculties are getting salary after one month. When an organisation uses supplier's credit and customers' advance to fulfill their day to day needs, it leads to a situation of lower or negative working capital. Banks, financial institutions, distributors, retailers with cash business or advance payment contract have negative working capital.

Normally, when we analyse working capital, it always refers to normal or positive working capital (excess or current assets over current liabilities). However, there are certain situations in which working capital is in negative form (excess of current liabilities over current assets). In that situation, how can a company manage liquidity with the negative working capital? In modern business, the concept of negative working capital is significant for the following reasons;

• It indicates operational efficiency of a corporate. That means without having or with low current assets the firm is managing day to day operations in an efficient manner. Eventually, it reduces cost of working capital and maximum earnings for the shareholders, which is the ultimate goal of the financial management.

• Concept of negative working capital is important to analyse liquidity position of corporate. When current assets are lower than current liabilities, what about the liquidity position of the corporate, how are they discharging current obligations in the short period. Traditionally, liquidity ratios are the measurement of liquidity of a firm with the ideal standard of 2:1. Negative working capital indicates lower cost of working capital (another way is higher profitability), but at the same time, it indicates poor liquidity (worried situation for the creditors, etc.) or we can say company is overburdened with current liabilities, which is not good for any situation (specially in a period of recession, etc).

• Another important impact of negative working capital is cash recovery or realisation situation. Negative working capital indicates quick realization of cash recourses (conversion of debtors in to cash) or one can say working capital cycle is shorter (for a days or maybe less than that). At the same time, payable policy of the company is to take longer time for payment against creditor. It indicates significant variations in the credit policy towards suppliers and customers.

To analyse, explain and focus on all these situations, a study of negative working capital and its impact on liquidity, profit earning capacity and overall impact on shareholders' value creation is important in the contemporary scenario.

NEGATIVE WORKING CAPITAL – HOW TO CREATE?

There are many ways to create negative working capital. Most important method is to minimise the size of current assets with favorable contract and agreement to the suppliers and other parties (to delay payments) and the same time, try to minimise credit facilities or maximise cash based business (collection of cash before the disbursement of actual payments to the various parties). When maximum customers are paying in advance, low or negative working capital is created. Another way to minimise the size of current assets is to adopt efficient collection method or brand oriented collection policy. Many companies are trying to minimise their cash resources with efficient utilisation of funds. Some companies are effectively using ERP system involving trade partners in planning and monitoring working capital items to reduce the level of working capital. Efficient cash collection and inventory management system provides an opportunity to run business with the negative working capital, because most of the suppliers are granting 30 days credit in general. Companies who are able to operate and maintain with negative working capital, have advantages to receive funds without cost as a form of credit from their suppliers which will enhance ROI in a significant manner. However, non availability of liquid resources is not a good situation at any time (especially in the stage of growth and boom).

OBJECTIVES

The basic objective of the study is to analyze and evaluate the impact of low or negative working capital on the profitability of the organization. The secondary objective is to know the answer of the question that the companies should avoid under-investment in working capital if they wanted higher profit margins as stated by the several researchers is essential for all the organization.

RESEARCH METHODOLOGY

A sample size of five Indian cement companies listed in BSE has been purposefully selected for the study purpose. The data for the study period 2000-2001 to 2009-10 have been collected from secondary sources i.e. Annual reports of the company as well as from the website moneycontrol.com. Keeping in view the scope of the study, it was decided to select five large companies on the basis of total assets and whose financial information is available for the entire study period so as to meet our requirements. Editing, classification and tabulation of the financial data collected from the above mentioned-sources have been done as per requirements of the study. The companies selected for study are Ambuja Cements Ltd., ACC Cement Ltd., India Cements Ltd., Madras Cements Ltd. and Shree Cements Ltd.

LIMITATIONS

We would like to make it clear that, mainly there are three limitations of this study, which are as under:

- The study is confined to ten years data only, i. e. from 2001–2010, therefore, a detailed analysis covering a lengthy period, which may give slightly different results has not been made.
- The study is based on secondary data collected from the website ***www.moneycontrol.com*** and the websites of sample companies; therefore the quality of the study depends purely upon the accuracy, reliability and quality of the secondary data source. Approximation, and relative measures with respect to the data source might impact the results.

The study is based on five companies of the Cement Industry in India that are also drawn from the companies listed in BSE. Therefore, the accuracy of results is purely based on the data of sample units. If one takes more sample units the results may go slightly differently.

HYPOTHESIS OF STUDY

On the basis of above mentioned objectives, the following hypotheses in the context of cement industry have been developed.

i) There is a direct and positive relationship exists between amount of working capital and profitability i.e. higher the working capital, higher is the profit and vice versa.

DETAILS OF SAMPLE COMPANIES

The following table shows the details of sample companies selected for study purpose:

TABLE – 1: DETAILS OF COMPANIES UNDER STUDY

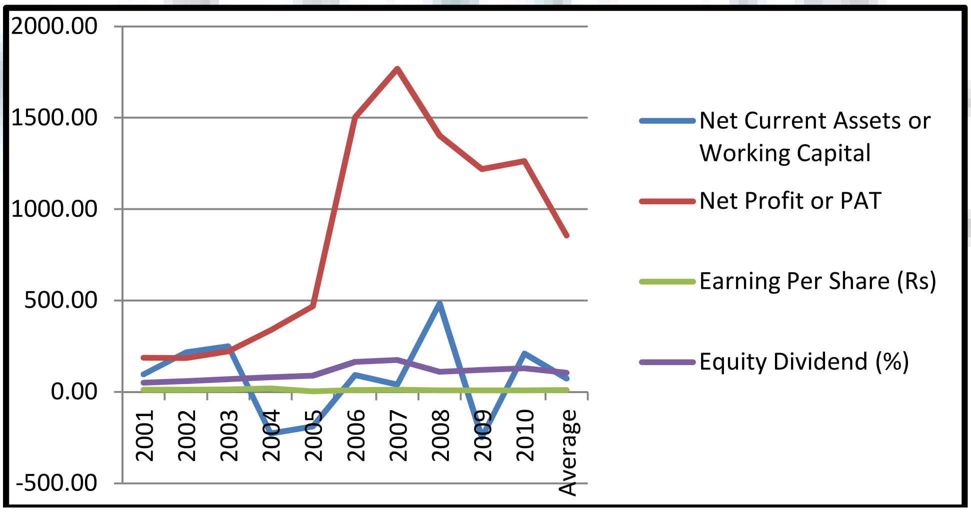
Sl. No.	Company Name	Total Assets as on 31-3-2010 (Rs. In Crores)	Size Group	Year of Incorporation	Age Group	State	Region
1	**Ambuja Cements**	7,395.13	Large	1981	New	Gujarat	West
2	**ACC**	6,993.31	Large	1936	Very Old	Maharashtra	West
3	**India Cements**	6,268.54	Large	1946	Very Old	Tamil Nadu	South
4	**Madras Cements**	4,124.67	Large	1957	Old	Tamil Nadu	South
5	**Shree Cements**	3,840.48	Large	1979	Old	Rajasthan	West

DATA ANALYSIS

To analyse the status of negative working capital and their impact on profitability, researcher has taken leading cement companies as a case study. Data for the last 10 years, were taken from 2001- 2010, to know the status of negative working capital and how it will affect the various earning variables such as PAT, EPS and DPS of the cement companies. Out of leading companies; status of Ambuja Cement, ACC, India Cement, Madras Cement, , and Shree Cement were analysed, to understand the nature and pattern of negative working capital and various aspect of earnings. Detailed analysis of negative working capital and various factors related to earning are as follows:

TABLE – 2: AMBUJA CEMENTS (Rs. In Crores)

Particulars	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Average
Net Current Assets or Working Capital	96.88	217.21	249.72	-226.64	-189.00	92.16	39.86	484.90	-247.59	210.27	72.78
Net Profit or PAT	186.35	186.15	221.73	336.79	468.29	1503.25	1769.10	1402.27	1218.37	1263.61	855.59
Earnings Per Share (Rs)	12.46	11.99	14.28	18.77	3.46	9.91	11.62	9.21	8	8.26	10.80
Equity Dividend (%)	50	60	70	80	90	165	175	110	120	130	105.00

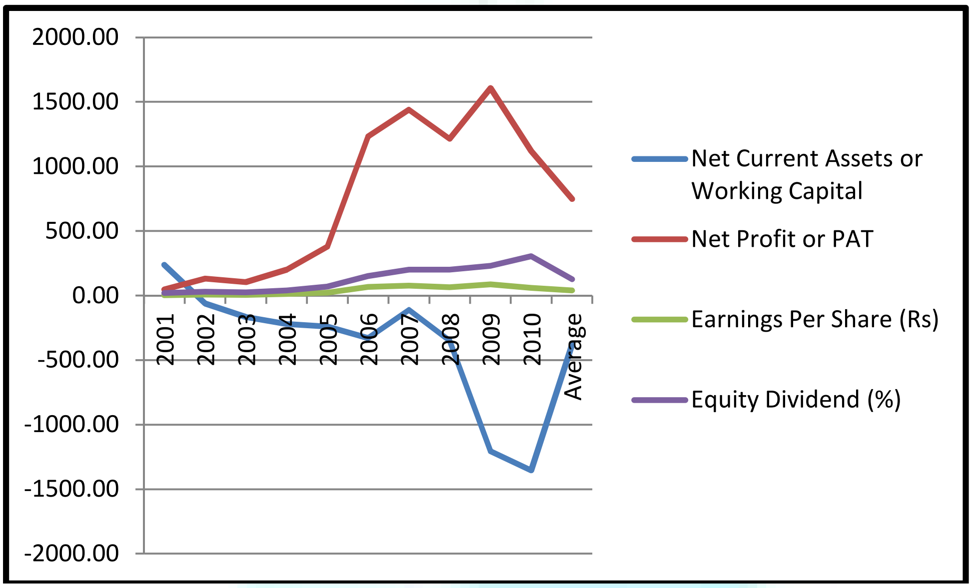


Source: Calculated and compiled from annual reports of Ambuja Cements from 2001 to 2010.

In case of Ambuja Cements, it has been found that, during the total study period of ten years, negative working capital has arisen three times in the years 2004, 2005 and 2009. In 2007 though the working capital is positive, it is too low which is less than the average. The impact of negative working capital for the year 2004 and 2005 is that the PAT, EPS and Rate of Dividend all are higher as compared to previous years except that in 2005 EPS is only Rs.3.46. This might be due to issue of new shares. In 2007 also, though the amount of working capital is less than the average, yet all the three parameters i.e. PAT, EPS, DP is more than the average. In 2009 also though the working capital is negative, it does not shows any negative impact on profitability. Rather the PAT, EPS and DP rates are as good as other years. Thus, it can be said that lower or negative working capital instead of adversely affecting the profitability, indicates efficiency in the operation as well as minimised cost of capital, which is important for shareholders value creation.

TABLE – 3: ACC CEMENTS (Rs. In Crores)

Particulars	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Average
Net Current Assets or Working Capital	238.58	-62.46	-165.16	-221.40	-239.40	-329.34	-110.86	-349.60	-1207.00	-1354.60	-380.12
Net Profit or PAT	47.48	130.43	103.89	200.24	378.39	1231.84	1438.59	1212.79	1606.73	1120.01	747.04
Earnings Per Share (Rs)	2.78	7.64	6.08	11.3	21.19	65.78	76.67	64.62	85.58	59.66	40.13
Equity Dividend (%)	20	30	25	40	70	150	200	200	230	305	127.00

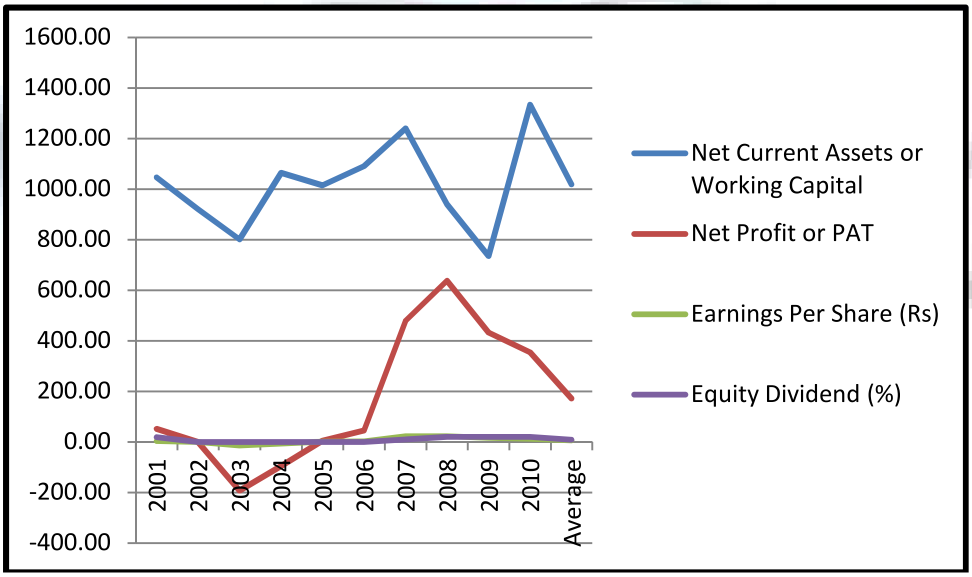


Source: Calculated and compiled from annual reports of ACC Cements from 2001 to 2010.

In case of ACC Cements, it has been found that, during the total study period of ten years, negative working capital has arisen all the years only except in 2001. The average working capital for the whole ten years is negative i.e. Rs. (380.12). Thus it can be said that the company has managed to run the business without any working capital for the entire period of study. But it is surprised to see that the impact of negative working capital on profitability is very much positive. There has been an increasing trend of PAT, EPS and DP Rate during the entire study period irrespective of prevalence of negative working capital. As the company is running with a negative working capital hence, lower cost of capital i.e. less financial burden for working capital finance and efficiency in the operations are key factors for higher profitability. Even with the lower liquidity the company is able to maintain earnings in the last one decade.

TABLE – 4: INDIA CEMENTS (Rs. In Crores)

Particulars	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Average
Net Current Assets or Working Capital	1046.70	921.35	800.64	1064.38	1014.87	1090.65	1240.52	940.16	734.60	1333.07	1018.69
Net Profit or PAT	51.15	-0.81	-193.17	-95.93	4.58	45.31	478.83	637.54	432.18	354.34	171.40
Earnings Per Share (Rs)	3.41	-0.26	-13.84	-6.87	0.33	2.38	21.73	22.62	15.3	11.54	5.63
Equity Dividend (%)	18	0	0	0	0	0	10	20	20	20	8.80

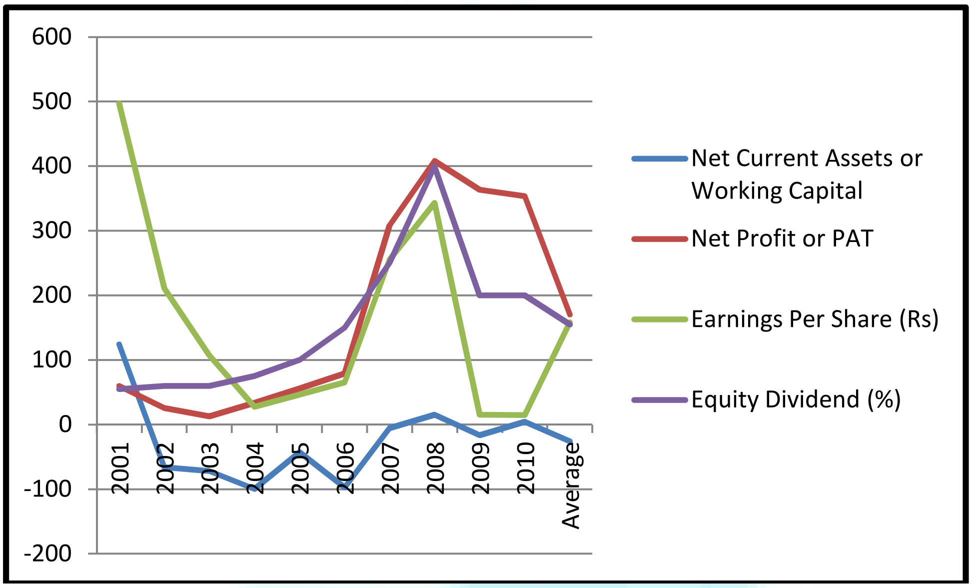


Source: Calculated and compiled from annual reports of India Cements from 2001 to 2010.

In case of India Cements, it has been found that, the company had a good amount of working capital in all the years from 2001 to 2010. There is no negative working capital at all. But the parameters of profitability are not impressive. The net profit i.e. PAT shows negative in three out of ten years i.e. in 2002, 2003 and 2004 and it is less than the average in six out of ten years. Similarly, the EPS also shows negative in same three years and it is also less than average in first six years of study. The rate of equity dividend is zero in five years starting from 2002 to 2006. For rest of the years the DP rate is also not that much attractive. Thus, it can be said that here positive working capital is not able to generate sufficient profit whereas in earlier cases companies with negative working capital could able to generate sufficient profit. Hence it cannot be said that there is a direct and positive relationship between working capital and profitability.

TABLE – 5: MADRAS CEMENTS (Rs. In Crores)

Particulars	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Average
Net Current Assets or Working Capital	124.02	-66.25	-71.91	-99.72	-42.96	-97.42	-5.56	15.12	-16.47	4.32	-25.68
Net Profit or PAT	60.04	25.52	12.96	33.40	55.92	79.02	308.02	408.29	363.52	353.68	170.04
Earnings Per Share (Rs)	497.19	211.37	107.32	27.65	46.3	65.43	255.03	343.02	15.28	14.86	158.35
Equity Dividend (%)	55	60	60	75	100	150	250	400	200	200	155.00

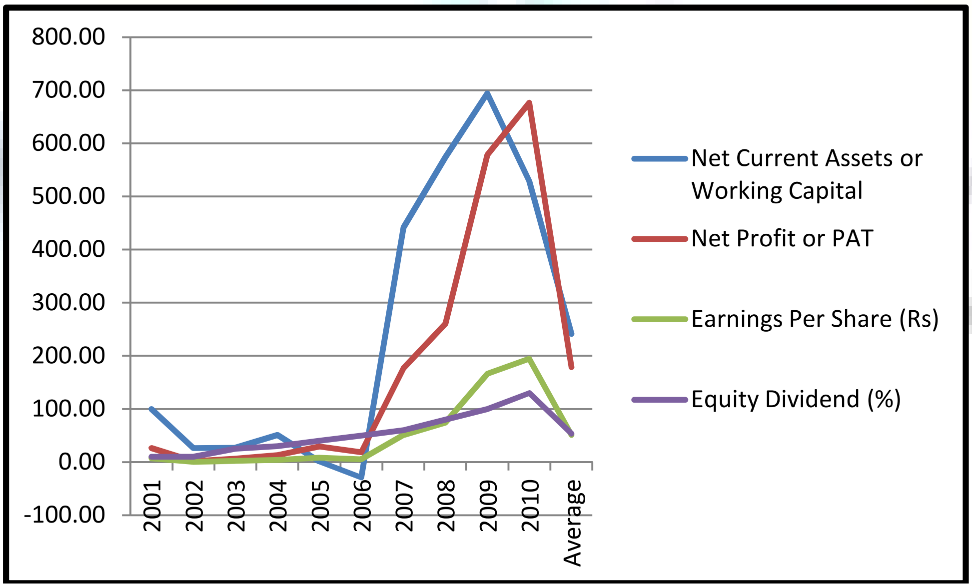


Source: Calculated and compiled from annual reports of Madras Cements from 2001 to 2010.

In case of Madras Cements, it has been found that, out of ten years the company has seen the negative working capital in seven years i.e. from 2002 to 2007 and in 2009. The average working capital for the entire study period is also negative which is Rs. (25.68) crores. In 2010 though it is positive, it is very low as compared to other years. But the fact to be noted here is that, having with negative working capital in most of the years, still the company is managed to generate profit and the profitability aspect is quite impressive. The PAT, EPS and DP Rate have shown an increasing trend, except a year or two. It indicates that even with the negative working capital (poor liquidity) their profitability and earnings are very higher, and it shows effective management of working capital as well day to day operation.

TABLE – 6: SHREE CEMENTS (Rs. In Crores)

Particulars	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	Average
Net Current Assets or Working Capital	99.42	26.27	27.12	50.71	0.84	-28.85	441.43	574.00	693.74	528.87	241.36
Net Profit or PAT	26.12	1.47	6.70	13.04	29.07	18.40	177.00	260.37	577.97	676.10	178.62
Earnings Per Share (Rs)	6.95	0.15	2.19	3.74	8.34	5.28	50.81	74.74	165.91	194.07	51.22
Equity Dividend (%)	10	10	25	30	40	50	60	80	100	130	53.50



Source: Calculated and compiled from annual reports of Shree Cements from 2001 to 2010.

In case of Shree Cements, it has been found that, only in 2006 there is negative working capital but for the first six years i.e. from 2001 to 2006 the company has a low working capital which is less than ten years average. Here the working capital and PAT goes in the same direction and with same proportion indicating that there exists a positive relationship between working capital and profitability.

CONCLUSION
After analyzing the data of all the companies, we can conclude that though there is a positive relationship between working capital and profitability, yet it does not hold good for all the cases and that too always. We have seen companies generating good profit with a negative working capital as well as companies not able to generate good profit even with having good amount of positive working capital. Hence we reject the null hypothesis that there is a direct and positive relationship exists between amount of working capital and profitability i.e. higher the working capital, higher is the profit and vice versa We have seen that the companies are having trend to use negative working capital to minimise the cost of borrowing for working capital. Whenever they are having trends of negative working capital, profitability is always higher (because of lower cost of interest and borrowings). Brand image of the products (intangible assets) enhances marketing efficiency and profitability (higher demand for the product). However, it can be said that negative working capital indicates non-liquidity or less liquidity within the firm which is not desirable at each and every stages of business.

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