INTERNATIONAL JOURNAL OF RESEARCH IN COMPUTER APPLICATION AND MANAGEMENT

CONTENTS

Sr. No.	TITLE & NAME OF THE AUTHOR (S)	Page No.
1.	ROBOT MANIPULATOR CONTROL USING INTELLIGENT CONTROL SCHEME *HIMANSHU CHAUDHARY, DR. RAJENDRA PRASAD & DR. N. SUKAVANUM*	1
2.	SECURITIZATION AS A FACTOR OF ECONOMIC INTEGRATION *DIVVIO GALLEGOS PANIAGUA & JOSE G. VARGAS-HERNANDEZ*	7
3.	E-GOVERNMENT - TRENDS AND CHALLENGES FROM THE PERSPECTIVE OF DEVELOPING NATIONS WITH FOCUS ON PAKISTAN *SHAKEEL IQBAL & DR. IJAZ A. QURESHI*	15
4.	INFLUENCE OF INTERNATIONAL LABOR MIGRATION AND REMITTANCES ON POVERTY REDUCTION IN BANGLADESH *MD. MORSHED HOSSAIN, MD. ZAHIR UDDIN ARIF & MD. NASIR UDDIN*	21
5.	APPLICATION OF SYSTEMATIC INNOVATION IN TECHNOLOGY DEVELOPMENT (RCA AND TOPSIS MODELS PRESENTATIONTO DETERMINEPROBLEM SOLVING STRATEGIES) *DR. YOUNOS VAKIL ALROAIA, JAVAD SOFIYABADI & ELAHEH BAKHSHIZADEH*	27
6.	FINANCIAL FLEXIBILITY AND RISK MANAGEMENT *MOZAFFAR A CHOWDHURY*	35
7.	BOARD DEPENDENCE, INTERNAL AUDITORS AND EARNINGS MANAGEMENT: AN EMERIACAL RESEARCH OF IRAN *MOHAMMADREZA ABDOLI, MARYAM SHAHRI & MOHSEN RAHMANI*	39
8.	CHILD LABOUR CONDITION IN RESTAURANT SECTOR OF BANGLADESH *JASMINE JAIM*	44
9.	FISCAL DEFICITS AND OUTPUT GROWTH IN NIGERIA *DR. FREDRICK ONYEBUCHI ASOGWA & MUSA SHERIFF URAMA*	47
10.	MEASURING THE QUALITY OF TEHRAN'S MUNICIPALITY SERVICES FROM THE VIEW POINT OF THE CLIENT *DR. AMIR HOSSEIN AMIRKHANI, SAYD MEHDI VEISEH, MARYAM GHASEMI & HAMIDEH SHEKARI*	52
11.	ATTITUDES OF INDIANS TOWARDS SERVICE QUALITY FOR LIFE INSURANCE IN INDIA *ANAND PRAKASH, SANJAY KUMAR JHA & S. P. KALLURKAR*	57
12.	PROFITABILITY PERFORMANCE: A CASE STUDY OF PANYAM CEMENTS AND MINERAL INDUSTRIES (AP), INDIA *N. VENKATA RAMANA, S. MD. AZASH & K. RAMA KRISHNAIAH*	64
13.	THE AUDIT EXPECTATION GAP: AN EMPIRICAL STUDY IN JORDAN *SULTAN HASSAN MOHAMMED AHMED & DR. D. RAGHUNATHA REDDY*	68
14.	DIFFUSION OF MOTOR VEHICLE SALES IN DELHI *DR. DEBABRATA DAS*	77
15.	AN EXPLORATORY INVESTIGATION ON EFFECTIVE RISK HANDLING ATTITUDES OF TOP BUSINESS LEADERS IN RELATION TO THEIR APPROACHES TOWARDS INNOVATION *DR. PUSHP LATA & ABHISHEK SYAL*	84
16.	AUTOMATIC INFORMATION COLLECTION & TEXT CLASSIFICATION FOR TELUGU CORPUS USING K-NN ALGORITHM *NADIMAPALLI V GANAPATHI RAJU, VIDYA RANI V, BHAVYA SUKAVASI & SAI RAMA KRISHNA CHAVA*	88
17.	RE-ATTEMPT CONNECTIVETY TO INTERNET ANALYSIS OF USER BY MARKOV CHAIN MODEL *DIWAKAR SHUKLA, KAPIL VERMA & SHARAD GANGELE*	94
18.	FACTORIAL STUDY OF STUDENTS ATTITUDE TOWARDS TECHNOLOGY ENABLED ACADEMIC LEARNING *SHARMILA.C & DR. R. RAJENDRAN*	100
19.	ATTITUDE AND PERCEIVED IMPORTANCE TOWARDS WORK-LIFE BALANCE POLICIES: A COMPARATIVE EMPLOYEE ANALYSIS OF PRIVATE AND PUBLIC SECTOR BANKS *S.M. SHARIQ ABBAS & VANDANA PREMI*	103
20.	AUDIENCE AWARENESS AND MULTICULTURAL COMMUNICATION *DR. DIVYA WALIA*	109
21.	FINANCIAL ANALYSIS OF INDIAN AUTOMOBILE INDUSTRY *DR. NISHI SHARMA*	112
22.	ANALYTICAL STUDY OF VARIOUS APPROACHES IN SERVICE QUALITY, DESIGN AND DEVELOPMENTS *DR. RAJESH N. PAHURKAR*	117
23.	WORK – FAMILY ROLE CONFLICT OF WOMEN TEACHERS IN ENGINEERING COLLEGES IN TIRUCHIRAPPALLI DISTRICT *DR. M. YASMIN & FAYAZ AHAMED .M.A.*	121
24.	INTERROGATION OF PACKAGING AND ADVERTISING *A.NITHYA*	125
25.	A COMPARATIVE STUDY OF THE DOT.COM CRISIS AND THE SUB-PRIME CRISIS *DR. T.GEETHA*	130
	REQUEST FOR FEEDBACK	136

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PROFITABILITY PERFORMANCE: A CASE STUDY OF PANYAM CEMENTS AND MINERAL INDUSTRIES (AP), INDIA

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ABSTRACT

Profitability analysis measures how will a firm is performing in terms of its ability to generate profits. Profitability of the firm is highly influenced by internal and external variables, i.e., size of organizations, liquidity management, growth of organizations, component of costs and inflation rate. The paper made an attempt to know the profitability and to assess the impact of selected profitability ratios on ROE of the company, for fulfillment of the objectives the data collected from the annual report from 2001-2010.the collected data is analyzed and computed to fit for drawing inferences .in this investigation correlation and multiple regression analysis was used to find out impact of selected profitability ratios (Gross Profit, Operating Profit, Net Profit, Earning Per Share, Return on Total Assets) on ROE. The result reveals that selected profitability ratios are not have significant impact on ROE

KEYWORDS

Earning per Share, Gross Profit, Net Profit, Operating Profit, Return on Total Assets, ROE.

INTRODUCTION

Profitability analysis measures how will a firm is performing in terms of its ability to generate profits. It is a financial metric that are used to assess business ability to generate earning as compare to expenses and other relevant costs incurred during a specific period of time. For most of these profitability ratios, having a higher value relating to a competitor's ratios or the same ratios from a previous period is indicative that the company is doing well. Profitability analysis helps the firm to take various strategic and operational oriented decisions such as net sales generated from the operation, gross profit figures in specific years compare to previous periods and also take the decisions relating to need for modernizations, expansion and diversification of business in the different markets.

Profitability ratios are used to give an idea of likely it is company turn a profits as well as how that profit relates to other important information about the company, in generally the higher a company's profit margin the company is in better in terms of sale, net profit and assets utilization so, there is special focus is made on profitability analysis. Profitability analysis is carries out with the help of different profitability ratios

LITERATURE REVIEW

The determinants of the profitability of Australian manufacturing firms analyzing to estimate the dynamic profitability models over the business cycle, to test both the persistence and cyclically of firm profitability. Econometric results suggest that lagged profitability is a significant determinant of current profit margins, and that industry concentration is positively related to firm profit margins. Also, profit margins are found to be procyclical in concentrated industries but counter-cyclical in less concentrated industries (McDonald, 1999).

The trade reforms are often expected to decrease profit margins as firms struggle to compete in international markets, there is the possibility that increased competition may improve firm efficiency and provide a positive impetus to firm profitability .the authors developed an efficiency index to directly analyze the impact of changing efficiency levels on firm profit margins (Kambhampati, 2003).

The determinant of profitability of Public Sector Banks in India by an empirical estimation of profit function model which showed that interest cost, interest income, other income, deposits per bank, credit to total assets, proportion of priority sector advances and interest income loss were the significant determinants of profits and profitability of Indian Public Sector Banks. Also, the average establishment cost positively contributed to the profitability but adversely affected the net profit of the Indian Public Sector Banks (Ganesan, 2001).

Assessed the financial performance (profitability) of commercial banks in Saudi Arabia. The authors employed a regression model to test the effect of business risk, concentration and market size on the profitability of the bank measured in terms of return on assets (ROA) and return on equity (ROE), and earnings per share (EPS). The empirical results generated from the three models showed that business risk and the bank size were the main variables which determined banks' profitability (Ahmed, 1999).

(Thomas, 1987) indicated that financial ratios express relationships among items taken from financial statements. The traditional use of financial ratios has been as a measure of the liquidity, performance and profitability of a firm and thereby as a monitor of the efficiency and effectiveness of the management

The profitability determinants into two main categories, namely the internal determinants and the external determinants. The internal determinants included management controllable factors such as liquidity, investment in securities, investments in subsidiaries, loans, non-performing loans, and overhead expenditure. Other determinants such as savings, current account deposits, fixed deposits, total capital and capital reserves, and money supply also play a major role in influencing the profitability of commercial banks. The external determinants include those factors which are beyond the control of management of these institutions such as interest rates, inflation rates, market growth and market share (Rasiah, 2010).

The superior firm hypothesis stating that firms differ with respect to their level of productivity and that these inter firm differences are the major factor behind profit heterogeneity. The logic behind it is that firms operating at relatively higher productivity levels have competitive advantages over less productive competitors which are reflected in their profitability Demsetz (1973).

On other hand few studied have identified and tested a number of factors affecting the profitability of business enterprises. Notable among them are Baker (1973), Phillips (1976), Rumelt (1982), Paul (1985), Brahmaiah (1991), Schwalback (1991), Kaur (1997), Sahu (2000), Vijayakumar and Kadirvrlu (2003), Raman and Dangwal (2003), Bhayani (2004 and 2006) and Mishra and Mishra (2006.

OBJECTIVES OF THE STUDY

- To know the profitability performance of Panyam Cements and Mineral Industries (AP), India, through profitability ratios.
- To assess the impact of profitability ratios on ROE with the help of multiple regression

HYPOTHESIS OF THE STUDY

H1: Gross Profit Ratio positively affects profitability
H2: Net Profit Ratio positively affects profitability
H3: Operating Profit positively affects profitability
H4: Return on Total Assets (ROA) positively affects profitability
H5: Earning Per Share (EPS) positively affects profitability

SCOPE OF THE STUDY

This study investigate the affect of selected profitability ratios on ROE, for this analysis data is gather from the annual financial statement of Panyam Cements and Mineral Industries (AP), India, from 2001-2010.

TOOLS OF ANALYSIS

In this study principal tool is used are selected profitability ratio such as Gross Profit, Operating Profit, Net Profit, Earning Per Share, Return on Total Assets and Return on Equity Ratios. The model is build based on selected profitability ratios (Gross Profit, Operating Profit, Net Profit, Earning Per Share, Return on Total Assets) are used independent variables and Return on Equity is used as dependent variable apart from ratios analysis statistical treatment of data are also performed among them Mean, Standard Deviation, Correalation, Multiple Regression analysis is carried out to draw out inferences for testing the hypothesis of the study.

OPERATIONAL DEFINITIONS

GROSS PROFIT MARGIN

Gross profit margin = sales-cost of sales/sales OR Gross profits/Sales. It measures the relative profitability of a firm's sales after the cost of sales has been deducted.The higher the gross profit margin, the better (that is, the lower the relative cost of the merchandise sold).

OPERATING PROFIT MARGIN

Operating profit margin = Operating Profits/sales. It measures the percentage of each sales amount remaining after all costs and expenses other than interest, taxes, and preferred stock dividends are deducted. It represents the pure profits earned on each sales amount. A high operating profit margin is preferred.

NET PROFIT MARGIN

Net profit margin = Earnings after Taxes (EAT)/Sales. It measures how profitable a company's sales are after all expenses, including taxes on interest and preferred stock dividends, have been deducted. The higher the firm's net profit margin, the better.

EARNINGS PER SHARE (EPS)

Earnings per share = Earnings after Taxes (EAT)/Number of shares of common stock outstanding. Earnings per share represent the number of amounts earned during the period on behalf of each outstanding share of common stock. The firm's earnings per share (EPS) are generally of interest to present or prospective stockholders and the management. EPS is closely watched by the investing public and is considered an important indicator of corporate success.

RETURN ON TOTAL ASSETS (ROA)

Return on Total Assets = Earnings after Taxes (EAT)/Total Assets. The return on total assets (ROA), often called the return on investment (ROI), measures the overall effectiveness of the management in generating profits with its available assets. The higher the firm's return on total assets, the better.

RETURN ON COMMON EQUITY (ROE)

Return on common equity = Earnings after Taxes (EAT)/ Common Stock Equity. The return on common equity (ROE) measures the return earned on the common stockholder's investment in a firm. Generally, the higher this return, the better off the owners.

FINDINGS AND IMPLICATIONS

Table no 1 shows correlation between ROE and Gross Profit it reveals that there is negative correlation between ROE and gross profit and which is insignificant at 5% level of significance hence, we reject hypothesis there is no influence of Gross Profit on ROE.

TABLE NO 1: CORRELATION BETWEEN GROSS PROFIT AND ROE

		ROE	GP
ROE	Pearson Correlation	1	-.199
	Sig. (2-tailed)		.582
	N	10	10
GP	Pearson Correlation	-.199	1
	Sig. (2-tailed)	.582	
	N	10	10

Table no 2 reveals correlation between operating profit and ROE and the Pearson correlation was used to test the H2: operating Profit Ratio positively affects profitability. The results reveal that operating profit is negatively correlated with return on equity (ROE) which is statistically insignificant at 5% level of significance.

TABLE NO 2: CORRELATION BETWEEN OPERATING PROFIT AND ROE

		ROE	OP
ROE	Pearson Correlation	1	-.216
	Sig. (2-tailed)		.550
	N	10	10
OP	Pearson Correlation	-.216	1
	Sig. (2-tailed)	.550	
	N	10	10

Table no 3 refers that correlation between Net Profit and ROE is negative correlation i.e -.215 which is insignificant correlation at 5% level of significance .The Pearson correlation was used to test the H3: Net Profit Ratio positively affects profitability, but in this test Net Profit not affect s positively on ROE

TABLE NO 3: CORRELATION BETWEEN NET PROFIT AND ROE

		ROE	NP
ROE	Pearson Correlation	1	-.215
	Sig. (2-tailed)		.551
	N	10	10
NP	Pearson Correlation	-.215	1
	Sig. (2-tailed)	.551	
	N	10	10

Table no 4 reveals that correlation between ROE and EPS is negative correlation i.e. -.073 which is insignificant correlation between ROE and EPS at 5% level of significance. This is used to test the H4: EPS positively affects profitability .As per Pearson correlation EPS is not positively affects on ROE

TABLE NO 4: CORRELATION BETWEEN EPS AND ROE

		ROE	EPS
ROE	Pearson Correlation	1	-.073
	Sig. (2-tailed)		.840
	N	10	10
EPS	Pearson Correlation	-.073	1
	Sig. (2-tailed)	.840	
	N	10	10

Table no 5 refers that correlation between ROE and ROA is -.084.To test the H5: ROA positively affects profitability. It is negative correlation between ROE and ROA which is insignificant correlation at 5% level of significance. So H5 rejected

TABLE NO 5: CORRELATION BETWEEN ROA AND ROE

		ROE	ROA
ROE	Pearson Correlation	1	-.084
	Sig. (2-tailed)		.817
	N	10	10
ROA	Pearson Correlation	-.084	1
	Sig. (2-tailed)	.817	
	N	10	10

Table no 6 reveals the result of multiple regressions the regression model used in this analysis is hereunder. ROE= β_0+ β_1 GP+ β_2 OP+ β_3NP+ β_4EPS+ β_5ROA,where β0, β_1, β_2, β_3, β_4 and β_5,are the parameters of the ROE line to be estimated. The pooled regression results of the model used to find out the impact of selected profitability ratios on ROE. In the pooled regression ROE is used as dependent variable and selected profitability ratios (Gross Profit, Operating Profit, Net Profit, Earning per Share, Return on Total Assets) are all the independent variables taken together and the impact of these independent variables on the ROE of the company. the multiple correlation and coefficient for all independent variable are Gross Profit (45.149), Operating Profit (-47.622), Net Profit (-3.894), Earning Per Share (39.048) and Return on Total Assets (.593) from these figures it is found that Gross Profit, EPS and Return on Total Assets are positively impact on the ROE of the company and remaining profitability ratios such as Operating Profit and Net Profit are negatively influence on ROE of the company. The multiple correlation co-efficient of ROE on Gross Profit, Operating Profit ,Net Profit ,Earning Per Share and Return on Total Assets is 0.350.it reveals that ROE is not highly influenced by selected profitability ratios in the study. It is also evident from the R^2 value that the independent variables gross profit, operating profit ,net profit ,earning per share and return on total assets contribute -97.5 percent of the variation on the ROE hence, it is inferred that selected profitability ratios are not shows the significant influence on ROE.

TABLE NO 6: MULTIPLE REGRESSION ANALYSIS

Variable	Regression Coefficient	Standard Error of Regression Coefficient	"t" Value	Sig.t
GP	45.149	79.625	.567	.601
OP	-47.622	105.440	-.452	.675
NP	-3.894	42.544	-.092	.931
EPS	39.048	255.114	.153	.886
ROA	.593	2.333	.254	.812
CONSTANT	-410.431	811.407	-.506	.640
multiple R=.350	R^2=.122	adj.R^2= -.975	S.E.of R=827.981	

CONCLUSION

Efficiency of any organization can be judge through its profitability. Profitability of the firm is highly influenced by internal and external variables, i.e., size of organizations, liquidity management, growth of organizations, component of costs and inflation rate. The results found that The multiple correlation co-efficient of ROE on Gross Profit, Operating Profit ,Net Profit ,Earning Per Share and Return on Total Assets is 0.350.it reveals that ROE is not highly influenced by selected profitability ratios in the study. It is also evident from the R^2 value that the independent variables Gross Profit, Operating Profit ,Net Profit ,Earning Per Share and Return on Total Assets contribute -97.5 percent of the variation on the ROE hence, it is inferred that selected profitability ratios are not shows the significant influence on ROE

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