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IMPACT OF WORKING CAPITAL MANAGEMENT ON CORPORATE PERFORMANCE: A STUDY BASED ON SELECTED BANKS IN NIGERIA

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ABSTRACT

Working capital is regarded as the lifeblood and nerve of a business, it is therefore essential to accommodate the smooth operations to any organizations. The objective of this study is to examine the impact of Working capital management on corporate performance of selected Nigerian banks. The study covers the period of ten (10) years 2005-2014. Data for the study were extracted from the firm's annual reports and accounts. Descriptive Research design was adopted for the study. Simple Random sample technique was used to select the samples. The performance was measured in terms of profitability by Return on assets as dependent variable and Working capital was determined by the Current ratio, Debtor's Collection Period ratio, Creditor's Payment Period ratio and Cash Conversion Cycle used as an independent variables and DR & BS as control variables. The data was analyzed using SPSS (version 21.0) and E-views using fixed effects model. Results of the analysis indicated that there is a strong positive and significant relationship between Current ratio &Cash Conversion Cycle with Return on assets while Debtor's Collection Period ratio & Creditor's Payment Period ratio has negative but significant relationship with Return on assets. In line with the above findings, the study suggested that the management should put more attention on their liquidity in order to maintain an adequate liquidity and ensure shorter time to cash conversion and also management should adopt a systematic and sound collection & payment policies for proper and operational efficiency and finally banks in trouble should be advised to merge or to be acquired by other mega banks.

KEYWORDS

working capital, working capital management, corporate performance and profitability.

INTRODUCTION

Every business firm requires two types of capital to run its business operations. i.e fixed capital and working capital. Fixed capital is that part of total capital which is used for purchase of fixed assets, diversification and expansion of business, renovation/modernization of plant & machinery. It is so called because; the assets in which it is invested are fixed in the sense that they are not meant to be removed from the business. Likewise, working capital is the portion of firm's total capital that is used for short term purposes i.e. to meet the financial requirement of the current operations. Working capital plays the same role in the business as the role of heart in the human body, just like heart gets blood and circulates the same in the body, in the same way, in working capital funds are generated and then circulated in the business. As and when this circulation stops, the business becomes lifeless. Thus prudent management of working capital is essential for the success of a business. The management of working capital includes the management of the level of current assets as well as the management of total working capital. Working capital refers to the capital that is required for day-to-day working in a business firm such as for purchasing raw-materials for meeting day-to-day expenditures on salaries, wages, rents, rates advertising etc. According to ICAI Working capital means the funds available for day-to-day operations of an enterprise. The term working capital is also known as revolving or circulating capital or fluctuating capital or short term capital. According to Gitman (2009) the objective of Working Capital Management (WCM) is to minimize the Cash Conversion Cycle (CCC) the amount of capital tied up in the firm's current assets. It focuses on controlling account receivables and their collection process, and managing the investment in inventory. Working capital management is vital for all business survival, sustainability and its direct impact on performance.

LITERATURE REVIEW

Aborode defines working capital management as the balancing of the liquidity and Profitability objectives of the firm as well as taking cognizance of risk. **Akpan** describes working capital management as the management of short-term financial resources of a company in a way that guarantees minimum cost of funds for profitability and the maintenance of a sizeable level of liquidity consistent with short-term obligation demands. **Pandey** defines working capital management as the administration of all current assets cash, marketable securities, accounts payable, bills payable, overdraft, etc.) with the focus of maintaining liquidity position of the firm. Working capital management (WCM) refers to all management decisions and actions that ordinarily influence the size and effectiveness of the working capital. WCM is an essential part of financial management and contributes significantly to a firm's wealth creation as it directly influences organizational profitability and liquidity. **Raheman and Nasr.** In summary, working capital management is concerned with the problem that arises in attempting to manage the current assets, current liabilities and the inter-relationship that exist between them. WCM means the deployment of current assets and current liabilities efficiently and effectively so as to maximize short-term liquidity and profitability.

Syed Ahsan Jamil, Mawih Alani and Faris Nasif Al shubiri, (2015), in their study titled "the effect of working capital (WC) management efficiency on the operating performance of industrial companies listed in the Muscat Securities Exchange (MSM) in Sultanate of Oman". The study employed an explanatory non-experimental research design. 37 out of 48 industrial companies listed in the MSM were taken. The study used the data contained in the annual reports of these companies for the period 2009-2013. The WC management efficiency is measured WC ratios such as cash conversion cycle, current ratio, current assets turnover, net WC ratio (NWCR), while the operation performance is measured by net operating profit (NOP) and earnings before interest and tax. The regression results revealed that the first model is significant and there are only cash conversion cycle and NWCR have impact on the NOP, but the second model is insignificant.

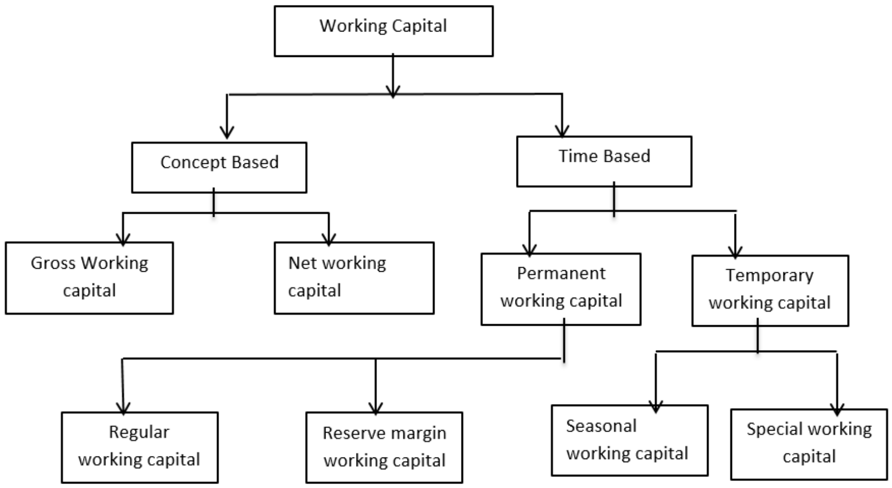
Adamu Yahaya and Hussaini Bala (2015), in their study titled "Working capital management and Financial Performance of Deposit Money Banks in Nigeria" The study examine the effect of working capital management of Deposit Money Banks in Nigeria. The study covers the period of six years 2007 to 2013. Data for the study were extracted from the firms' annual reports and accounts. After running the OLS regression, a robustness test was conducted for validity of statistical inferences, the data was empirically tested between the regressors and the regressed, a multiple regression was employed to test the model of the study using OLS. The results from the analysis revealed a strong positive relationship between current ratio and quick ratio and ROA of Listed Deposit Money Banks in Nigeria, while cash ratio was found to be inversely but significantly related to ROA of Listed Deposit Money Banks in Nigeria.

Muzaffar Asad and Hassan Qadeer, (2014), in their work titled "Components of working capital and profitability: A case of fuel and Energy sector of Pakistan" analyzed the impact of components of working capital on the profitability of fuel & energy sector of Pakistan. Initially six (6) variables have been taken & panel data analysis has been applied to identify their significance. Results revealed that fixed effect model is an appropriate model based on Hausman test. Further, debt ratio, current ratio and company size have significant impact on the profitability.

Mohammad Shaukat Malik and Mahum Bukhari, (2014),in their research work titled "The Impact of Working Capital Management on Corporate Performance :A study of Firms in Cement, Chemical and Engineering Sectors of Pakistan" the study investigate the impact of working capital management (WCM) on corporate performance in cement, chemical and engineering sectors of Pakistan. Data is obtained from annual reports of the companies during 2007-2011. Pooled ordinary least squares method is used to estimate the relationship between the measures of working capital management and performance. WCM measures include average age of inventory, average collection period, average payment period, operating cycle, and the cash conversion cycle whereas return on equity is used as a measure of firm performance. Leverage and firm size are taken as control variables. Results indicate that average payment period negatively and significantly whereas cash conversion cycle positively and significantly relate with return on equity. While, average collection period and operating cycle positively and insignificantly whereas average age of inventory negatively and insignificantly relates to the return on equity. In short WCM influences the corporation's performance. In summary, working capital management is concerned with the problem that arises in attempting to manage the current assets, current liabilities and the inter-relationship that exist between them. WCM means the deployment of current assets and current liabilities efficiently and effectively so as to maximize short-term liquidity and profitability. The above review shows that there is a positive and significant relationship between working capital management and corporate performance of corporations.

CLASSIFICATION OF WORKING CAPITAL
Working capital can be classified into two ways, i.e. concept based and Time based working capital.

FIGURE 1: CLASSIFICATION OF WORKING CAPITAL



1. **CLASSIFICATION BASED ON CONCEPT. INCLUDES THE FOLLOWINGS**

(a) Gross working capital: It refers to the firm's investment in current assets. Current assets are the assets that are to be converted into cash within an accounting year and includes cash in hand, cash at bank, debtors, short term securities, bill receivable, stock and prepaid expenses. According to this concept, working capital means gross working capital which is the total of all current assets of a business. It can be represented by the following equation.

Gross working capital =Total current assets

(b) Net working capital: It refers to excess of total current assets over total current liabilities. In other words, the difference between current assets and current liabilities can be taken as Net working capital. Current liabilities refer to those liabilities which are repayable within an accounting year and includes creditors, bill payable, bank overdraft, short term loans, outstanding expenses, provision for tax, proposed and unclaimed dividends. Net working capital can be positive or negative. A positive net working capital will arise when current assets exceed current liabilities. A negative net working capital occurs when current liabilities are in excess of current assets. Net working capital can be represented through the following equation.

Net working capital = current assets –current liabilities

2. **CLASSIFICATION BASED ON TIME**

From the point of view of time, the term working capital can be classified into two categories i.e. permanent working capital and Temporary working capital.

(a) Permanent working capital: This refers to that minimum amount of investment in all current assets which is required at all times to carry out minimum level of business activities. In other words, it represents the current assets required on a continuing basis over the entire year. Permanent working capital is permanently required for the business and therefore it should be financed out of long term sources such as share capital, debentures and long term loans. This capital can be subdivided into two (2) i.e. Regular working capital and Reserve margin or Cushion working capital.

i) Regular working capital: It is the minimum amount of liquid capital needed to keep up the circulation of the capital from cash to inventories to receivables and back again to cash. This would include a sufficient cash balance in the bank to pay all bills, maintain adequate supply of raw materials for processing, carry a sufficient stock of finished goods to give prompt delivery etc.

ii) Reserve margin or Cushion working capital: It is the excess over the need for regular working capital that should be provided for contingencies that arise at unstated period. The contingencies include rising price, business depression, strikes, fires and unexpectedly severe competition.

(b) Temporary working capital: It refers to that part of total working capital which is required by a business over and above permanent working capital. It is also called variable working capital. Since the volume of temporary working capital keeps on fluctuating from time to time according to the business activities, it may be financed from short term sources. It is further subdivided into two i. seasonal working capital and special working capital.

i) Seasonal working capital: It is the additional amount of current assets particularly cash, accounts receivables and inventory which is required during the more active business seasons of the year.

ii) Special working capital: It is required for financing special operations such as extensive marketing campaigns, experiments with product or methods of production, carrying of special jobs.

IMPORTANCE OF THE STUDY
Working capital management means management of current assets and current liabilities and financing these current assets. If these firms properly manage their cash, accounts receivables, accounts payables and inventories in a proper way, will ultimately increase profitability and corporate performance of these companies.

STATEMENT OF THE PROBLEM
A study of working capital is of major importance to internal and external analysis because of its close relationship with the current day-to-day operations of a business. As pointed out by **Ralph Kennedy and Steward McMuller,** the inadequate or mismanagement is the leading cause of business failure which are used in or related to current operations and represented at any one time by the operating cycle of such items as against receivables, inventories of raw-materials, stores, work-in-progress and finished goods, merchandise, notes or bill receivables and cash.

OBJECTIVES OF THE STUDY

1. To analyze the impact of various components/aspects of working capital on Return on assets (ROA) of selected Nigerian banks
2. To examine whether working capital management of selected Nigerian banks. has impact on its performance.

HYPOTHESES OF THE STUDY

In order to fulfill the objectives of the study, the following Null hypotheses (Ho) were formulated.

Ho_2: There is no significant relationship between working capital management components and corporate performance of selected Nigerian banks.

Ho_1: There is no significant relationship between working capital management and corporate performance of selected Nigerian banks.

RESEARCH METHODOLOGY

DATA COLLECTION AND ANALYSIS

The Research design used for the study is Descriptive Research design as it helps to provide a comprehensive and details explanation of the phenomena under the study. The research method adopted was Descriptive statistics and Regression Analysis, through running and comparing the Fixed Effect Model (FEM) and Random Effects Model (REM) and then Fixed Effects Model were chosen after Hausman Test was carried out. FEM allows for heterogeneity or individuality among the items under study by allowing having its own intercept which is time invariant. The population of the study consists of all the sixteen (16) banks listed in the Nigerian Stock Exchange (NSE) as recorded by its website. The sample technique used is simple Random in which ten (10) banks were selected. The data was Panel data which was extracted from Secondary source through Annual reports and Accounts of the sampled banks for a period of ten (10) years starting from 2005-2014. Eviews-8 was applied using Fixed Effects Model and Statistical Packages for Social Science (SPSS) (Version 21.0) was applied also to get the results.

DEPENDENT VARIABLE

Dependent Variables are variables that are used to measure the performance of firms. Financial ratios are uses to compare different companies in the same industry, to compare different industries and over a period of years, a firm or an industry develops certain norms that may indicate future success or failure. It is measured as Return on Assets.

INDEPENDENT VARIABLES

The following are the independent variables used in this study. Current ratio, Debtor's collection Period Ratio, Creditor's Payment Period Ratio and Cash conversion cycle.

CONTROL VARIABLES

In order to have a reliable analysis of the impact of working capital management performance on profitability, it is common in working capital literature to use some control variables to account for various factors that may influence profitability of firms (Deelof, 2003; Eljelly, 2004; Lazaridis and Tryfonidis, 2006; Padachi, 2006; Afza and Nazir, 2007; Tewodros 2010;). Accordingly, together with the above working capital variables, some control variables that are specific to firms and general to the economy as a whole were taken into account in this study. Such variable are: Debt Ratio and Bank size.

SUMMARY OF VARIABLE AND MEASUREMENT

MODEL SPECIFICATION

Model 1

ROAit = βo+β1(CRit) +β2(DCPRit)+ β3 (DRit) +β4(BSit) + µit

Model 2

ROAit = βo+β1(CPPRit) +β2(CCCit)+ β3(DRit) +β4(BSit) + µit

RESULTS AND DISCUSSION

This section presents the regression result of the dependent variable (ROA) and the independent variables of the study (CR, DCPR, CPPR and CCC) and control variables (DR and BS). The presentation was followed with the analysis of the association between dependent variable and each individual independent variable and also a cumulative analysis was also captured.

SUMMARY OF REGRESSION ANALYSIS

TABLE 1

Variables	Coefficient	Std. Error	t-Statistics	P-value
Constant	1.535	2.679	0.57	0.5682
CR	0.018	0.038	0.476	0.0351
DCPR	-2.60	5.39	0.483	0.0303
CPPR	-4.88	1.67	-0.292	0.0078
CCC	3.79	5.94	0.638	0.0252
DR	1.952	0.167	11.712	0.0000
BS	-0.09	0.157	-0.614	0.5410

Sources: Computed by the researcher 2016 from E-views 8

R2 0.6689

Adjusted R2 0.6233

F-Statistics 14.6527

F-Significance 0.0000

The cumulative R2 is the coefficient of multiple determination, it shows the extent to which variation in dependent variable is been explained by independent variable. Results from the estimate shows that 66.90% variation in Return on Asset (ROA) is been explained by Current rario(CR), Debtor's collection period ratio(DCPR), Creditor's Payment period ratio(CPPR) & Cash conversion cycle(CCC). The F-statistics of 14.65 shows that the overall model fit the data well. This indicates that the independent variables are properly selected, combined and used. It implies that for any change in working capital management of Nigerian banks, their ROA will be directly affected. The value of F-statistics which was statistically significant at a level of 0.0000 means that, there is 99.99% probability that the relationship among the variables was not due to mere chance.

From the table above, t-value for current ratio was 0.48 & the coefficient value of 0.018 with significant value of 0.0351. This signifies that CR is positively, strongly and significantly influencing the ROA of selected banks in Nigeria. DCPR has a t-value of 0.48 and coefficient value of -2.60 with significant value of 0.0303. This signifies that DCPR is negatively and significantly affects the profitability of the banks. CPPR has a t-value of -0.29 and coefficient value of -4.88 with significant value of 0.0078. This shows that CPPR has significantly but negative impact on profitability of the banks. CCC has t-value of 0.64 and coefficient value of 3.79 with significant value of 0.0252. This shows that CCC has significant and positive impact on profitability of the banks in Nigeria. While other control variables of Debt ratio have a coefficient value of 1.95 with significant value of 0.0000. It shows that it has some significant in controlling the models of the study and Bank Size is negatively and statistically insignificant as it can be observed from the regression result above with a beta coefficient of -0.09 and p-value of 0.59. This shows that even without controlling for bank size, the models of the study can stand.

FINDINGS

Current ratio was found to be significant and positive associated with ROA at 5% level of significance indicating that larger proportion of CR increases the Return on assets of selected Nigerian banks and therefore Null hypothesis is hereby rejected. DCPR was found to be significant but negatively associated with the ROA at

5% level of significance, indicating that the lower the DCPR the higher the profitability and vise-vasa. Null hypothesis is therefore rejected. CPPR was found to be statistically significant but negatively associated with the ROA at 5% level of significance, indicating that the lower the CPPR, the higher the profitability through getting the benefits of early payment and vice-vasa. Null hypothesis is hereby rejected. CCC found to have positive and statistically significant associated with ROA at 5% level of significance. It means it is significantly associated with the profitability of selected Nigerian banks, it provides an evidence of rejecting Null hypothesis.

RECOMMENDATIONS

1. The management should put more attention on their liquidity in order to maintain adequate liquidity in the sector because the regression result of the study has empirically proved that, higher the CR the more the profitability, so as a result of this the Nigerian banks should invest more in current asset as it have positive impact on profitability.
2. The management should adopt a systematic and sound collection policies in order to minimize the total debts and hence improve the overall performance of the banks, as it was empirically proving that lower collection period will increase in profitability and on the other hand it decreases the profitability.
3. The management should continue to ensure prompt and early payments of debts as it will create a cordial relationship with creditors as revealed by the study
4. The management should ensure that cash conversion cycle shall not take a longer period as it will affect the profitability negatively.
5. Bank management should make WCM as an integral function of financial or risk Department, where working capital components can be effectively and efficiently managed for the successful operations of the activities.
6. Banks in trouble should be advised to either merge or to be acquired by other mega bank in order to enhance the efficient management of the banking activities.

CONCLUSIONS

Working capital plays a vital role in the company's operations and requires efficient and effective management. The management of working capital concerns the management of cash, account receivable, account payable and cash conversion cycle. It's necessary for a company to monitor its balance at the appropriate level. Shortage of working capital may lead to lack of liquidity as well as a loss of production and sales, on the contrary case, excess balance of working capital could be seen as loss of investment opportunities. One way to achieve the objective of having efficient working capital is to manage short-term assets and liabilities such as implementing policies on credit policy, collection policy as well as payment terms. The study used Descriptive statistics and Regression analysis using Fixed Effects Model (FEM). The result of fixed effects regression indicates that the bank's profitability is statistically significant and positive influence by CR & CCC, while DCPR & CPPR is significantly and negative influence to the profitability. However, the DR used as control variable in this study was concluded to have a statistically significant and positive influence on the profitability of the Nigerian banks while BSas a control variable was concluded not to have any significant influence on the profitability of the Nigerian banks. Therefore, BS is not a major determinant factor of bank's performance.

LIMITATIONS

1. Data Availability: Some banks may have incomplete relevant data required for the studies.
2. The study is limited to particular sector i.e. Nigerian banks.
3. Also findings and recommendations is only applicable to those banks as working capital management varies in other sectors.

SCOPE FOR FURTHER RESEARCH

Future research should investigate on how to generalize the findings be young the Nigerian banks listed in the Nigerian Stock Exchange (NSE). Researchers should also attempt to investigate the banks not listed in NSE for generalization of findings. Further studies could be a study to examine an impact on other measures of working capital management and explore a relationship with other factors such as economy.

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