THINK INDIA JOURNAL

ISSN:0971-1260

Vol-22-Issue-10-November-2019

Short Term Capital Management

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Abstract:

Management is an art of anticipating and preparing for risk, uncertainties and overcoming obstacle. Working capital is as lifeblood of a business. Its effective provision can ensure the success of a business, while its inefficient management can lead not only to loss of profit but also to the ultimate downfall of what otherwise might considered as a promising concern. A study of working capital is of major importance to internal and external analysis because of its relationship with the current day to day operations of a business. In this project the theoretical background include meaning of working capital, types of working capital, importance of working capital and working capital cycle. The data analysis includes calculation and projection of future working capital requirement, working capital element, working capital ratio analysis, their interpretation. 3

Key Words: Operating Cycle, Current asset and Current Liabilities , Income Statement

Introduction:

Management is an art of anticipating and preparing for risk, uncertainties and overcoming obstacles. An essential precondition for sound and consistent assets management is establishing the sound and consistent assets management policies covering fixed as well as current assets. In modern financial management, efficient allocation of funds has a great scope in finance and profit planning, for the most effective utilization of enterprise resources, the fixed and current assets have to be combined in optimum proportions.

Working capital is as lifeblood of a business. Its effective provision can ensure the success of a business, while its inefficient management can lead not only to loss of profit but also to the ultimate downfall of what otherwise might considered as a promising concern. A study of

ISSN:0971-1260
Vol-22-Issue-10-November-2019

working capital is of major importance to internal and external analysis because of its relationship with the current day to day operations of a business

Review of Literature:

1. Bhatt V. V. (1972) widely touches upon a method of appraising working capital finance applications of large manufacturing concerns. It states that similar methods need to be devised for other sectors such as agriculture, trade etc. The author is of the view that banks while providing short-term finance, concentrate their attention on adequacy of security and repayment capacity. On being satisfied with these two criteria they do not generally carry out any detail appraisal of the working of the concerns.

Purpose of the study:

- To understand meaning and importance of Working Capital.
- To analyze various methods of calculating of Working Capital.
- To find out the relationship of Working Capital with another components.
- To study the various aspects of Working Capital.
- To find out the Working Capital requirement of **Jyoti International Foods Pvt. Ltd.**..
- To make observations and suggestions after understanding the trends in Working Capital.
- To find out the Working Capital requirement Of **Jyoti International Foods Pvt. Ltd.**

RESEARCH METHODOLOGY:

The methodology used in the project is analytical. The Data is obtained from secondary sources. Annual reports and internet are the main sources of data collection.

Data Analysis:

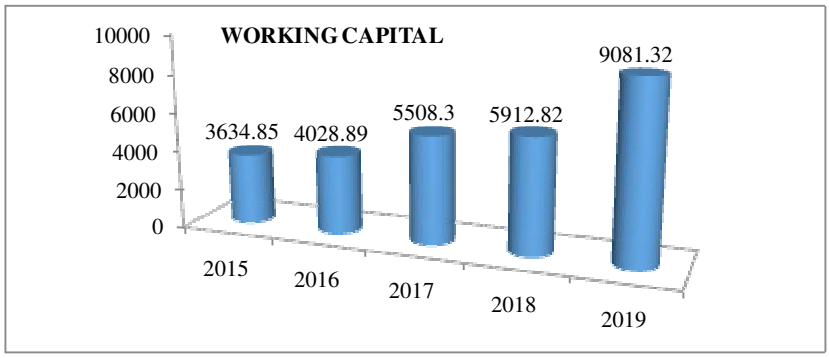
CALCULATION OF WORKING CAPITAL REQUIREMENT AS PER BALANCE SHEET OF AWL.

Table No. 1 - Working Capital

WORKING CAPITAL STATEMENT OF JYOTI INTERNATIONAL FOODS PVT. LTD.					
Current Assets	As on 31.03.2015	As on 31.03.2016	As on 31.03.2017	As on 31.03.2018	As on 31.03.2019
Current Investments				2,518.22	3,276.69
Inventories	3,361.69	3,580.87	3,799.16	4,908.54	5,322.26

ISSN:0971-1260
Vol-22-Issue-10-November-2019

Sundry Debtors	2,296.23	1,306.63	2,627.34	3,122.05	3,657.54
Cash and Bank Balances	640.3	747.97	1,302.45	629.70	534.29
Loans and Advances	1,356.75	2,126.40	1,461.14	799.39	939.52
Other Current Assets				804.72	980.34
Total C. A. (A)	**7,655.00**	**7,761.87**	**9,190.09**	**10,427.74**	**14,710.64**
Current liabilities					
Current Liabilities	2,244.11	2,647.51	2,350.15	3,110.46	3991.76
Provisions	1,776.04	1,085.67	1,331.64	1,404.46	1,637.56
Total C. L. (B)	**4,020.15**	**3,733.18**	**3,681.79**	**4,514.92**	**5,629.32**
Net Working Capital (Net Current Assets)	**3,634.85**	**4,028.69**	**5,508.30**	**5,912.82**	**9,081.32**



Graph No. 1 - Working Capital

INTERPRETATION:

- From the above graph the requirement for working capital is showing an increasing trend, this shows that the company need for working capital has been increased due to expansion in business and growth in sales.
- An increase in working capital indicates that the business has either increased current assets (that is has increased its receivables, or other current assets) or has decreased current liabilities, **for example** has paid off some short-term creditors.

ISSN:0971-1260
Vol-22-Issue-10-November-2019

- For the year 2018 the company has not taken any loan since funds were sufficient for working capital requirement

OPERATING CYCLE

Operating cycle is calculated as follows = **Raw Material + WIP Days + Finished Goods Days + Debtors Days – Creditors Days**

Operating Cycle for the year 2014-15

Raw Material= (Average Raw Material / Raw Material Consumed) * 365

= (1046.41 / 14342.55)* 365

= (0.11) * 365

= 26.63 days i.e. 27days

Work in Progress = (Average W I P / Total Cost of goods)*365

= (815.26 / 14496.02)*365

= ()*365

=20.53 days i.e. 21 days

Finished Goods Holding Period = (Average Stock / Total Cost of Goods Sold) * 365

= (1168.08/ 14496.02) * 365

= (0.12) * 365

= 29.41 days i.e. 30 days

Debtors Collection Period = (Debtors / Net Sales)*365

= (2296.23 / 26054.8)*365

= (0.09)*365

= 32.17 days i.e. 33 Days

Creditors Credit Period = (Creditors / Material cost)*365

= {1788.35 / 14342.55}*365

= (0.12)*365

= 45.51 days i.e. 46 days

ISSN:0971-1260
Vol-22-Issue-10-November-2019

Net Operating Cycle = Raw Material Holding Period + WIP Days + Finish Goods Days + Debtors Collection Period – Creditors Credit Period

= 27 days + 21 days + 30 days + 33 day – 46 days

= 65 Days

Operating cycle period of **JYOTI INTERNATIONAL FOODS PVT. LTD.** in year 2014-15 is 65 days. It means that company needs 65 days to get his money back from the operations. It means that there are 365 / 65 = 5.61 operating cycles are completed in one year.

INTERPRETATION:

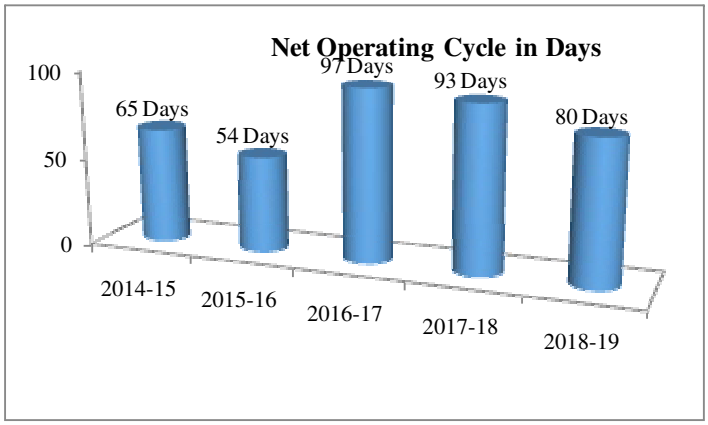
- In above figure shows that company holds raw material on average for 27 days, it gets credit from the supplier for 46 days, finished goods are held for 30 days & 33 days credit is extended to debtors.
- The total days are 104, i.e., 41 + 46 + 43 + 33 - 30 days is the total of working capital operating cycle in year 2014-15, it is also called as Net Operating Period. And it shows the 5.61 Operating Cycles within a year.
- Thus the working capital cycle helps in the forecast, control & management of working capital.
- It indicates the total time lag & the relative significance of its constituent parts. The duration may vary depending upon the business policies. In light of the facts discusses above we can broadly classify the operating cycle of a firm into three phases viz.

Table No. 2 – Operating Cycle

NET OPERATING CYCLE JYOTI INTERNATIONAL FOODS PVT. LTD.					
(A)Current Assets, loans & advances	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Raw Material (R.M)	27 days	33 days	37 days	40 days	37 days
Work in progress (WIP)	21 days	23 days	20days	18 days	14 days
Finish Goods (F.G)	30 days	38 days	28 days	25 days	28 days
Sundry Debtors (Deb)	33 days	22 days	37 days	39 days	40 days
Total (A) / Gross Operating Cycle	**111** days	**116** days	**122** days	**122 days**	**119 days**
(B)Current Liabilities					
Creditors	46 days	62 days	25 days	29 days	36 days

ISSN:0971-1260
Vol-22-Issue-10-November-2019

Total (B)	46 days	62 days	25 days	29 days	**36** days
Net Operating Cycle (A-B)	**65** days	**54** days	**97** days	**93** days	**80 days**
Operating Cycles Within Year	**5.60**	**6.76**	**4.07**	**3.92**	**4.56**



Graph No. 2 – Net Operating Cycle

ITERPRETATION:

- From the above graph Net Operating Cycle is not fixed every year, it is changed year by year.
- Net Operating Cycle is decreasing form year 2014-15 to 2015-16 and also 2016-17to 2017-18.
- In year 2014-15 the Net Operating Cycle is very high.
- When the Net Operating Cycle of the company is increased the Operating Cycles within year is decreased. It can be seen from the graph that the Net Operating Cycle of the company for 2014-15, 2015-16, 2016-17, 2017-18 and 2018-19 were 65 days, 54 days, 97days, 93 days, 80 days respectively.
- And the Operating Cycles within the year are 5.6, 6.67, 4.07, 3.92, and 4.56 respectively.

CURRENT RATIO: This ratio is calculated by dividing the current assets by current liabilities. Current ratio is also called as solvency ratio, as it indicates how the expected current claims are covered by current assets. This ratio is calculated with the help of the following formula:

CURRENT RATIO = CURRENT ASSETS / CURRENT LIABILITIES.

ISSN:0971-1260
Vol-22-Issue-10-November-2019

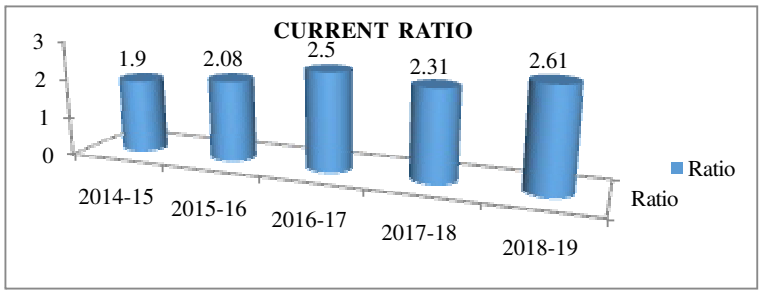
* **CURRENT ASSET:** Current asset means assets which have been purchased in order to convert them into cash or current assets within a period of normally one accounting year. These **assets include cash andbank balance, short term investment, bills receivables, debtors, short term loans, inventories and pre-paid expenses.**

***CURRENT LIABILITIES:** Current liabilities means those liabilities with a short term duration , which is normally up to one year from the date of creation and are paid out of existing current assets or by creating a new current liability. These **liabilities includes , bank overdraft , bills payable , creditors , provision for taxation , outstanding interest , advance payment received and portion of a debt expected to mature within a period of one year.**

The following data is extracted from records of the company:

Table No.3 - Current Ratio

Particulars	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Current Assets (Rs. in lacs)	7655.00	7761.87	9190.09	10427.74	14710.64
Current Liabilities (Rs. in lacs)	4020.15	3733.18	3681.79	4514.92	5629.32
Current Ratio	**1.9**	**2.08**	**2.5**	**2.31**	**2.61**



ISSN:0971-1260
Vol-22-Issue-10-November-2019

Graph No.3 - Current Ratio

INTERPRETATION:

- This ratio indicates the coverage of current assets to the current liabilities.
- Normally it is expected that the current assets should be **2:1**, which indicates that current assets should be twice as compared to the current liabilities.
- The current ratio can give a sense of the efficiency of a company's operating cycle or its ability to turn its product into cash.
- When the current asset of the company is increased the working capital of company also increases. It can be seen from the graph that the current ratio of the company for 2014-15, 2015-16, 2016-17, 2017-18 and 2018-19 were 1.9**:**1; 2.08**:**1, 2.5:1 & 2.31:1 and 2.61:1 respectively.
- Also a company's ratio differs from the industry ratio because of its different policy.
- For the year 2017-18, **JYOTI INTERNATIONAL FOODS PVT. LTD.** has sound liquidity position as current asset are more than current liabilities.
- It is advice to maintain the same in future provided inventory form less percentage of current assets

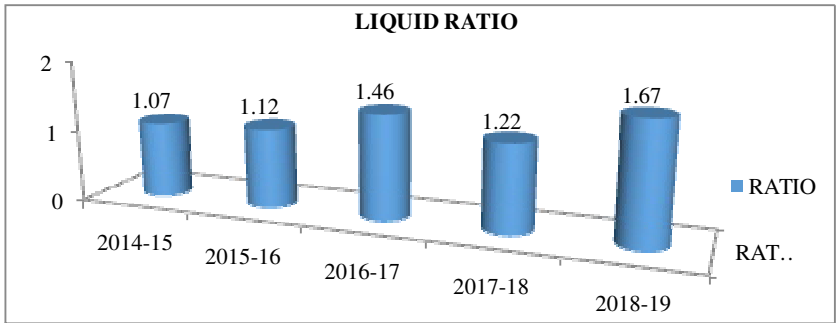
LIQUID RATIO = LIQUID CURRENT ASSETS / LIQUID LIABILITIES:

The following data is extracted from reports of the company:

Table No.5 - Liquid/Acid/Quick Ratios

Particulars	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Liquid Current Assets (Rs. in lacs)	4293.31	4181	5390.93	5519.2	9388.38
Liquid Current Liabilities (Rs. in lacs)	4020.15	3733.18	3681.79	4514.92	5629.32
Ratios	**1.07**	**1.12**	**1.46**	**1.22**	**1.67**

ISSN:0971-1260
Vol-22-Issue-10-November-2019



Graph No.4 - Liquid/Acid/Quick Ratios

INTERPRETATION:

- A quick ratio of 1:1 or more is considered as satisfactory or of sound liquidity position.
- Quick ratio for the year 2014-15, 2015-16, 2016-17, 2017-18 and 2018-19 were 1.07:1, 1.12:1, 1.46:1, 1.22:1 and 1.67:1 respectively.
- The Company's ratio is more than ideal ratio that means its liquidity position is good.
- The company carries out the production activity as per the projects available and only machines [finished goods] are kept as finished goods in inventory; the data signifies that the company has enough capacity to pay of its short term obligations.

WORKING CAPITAL TURNOVER RATIO:

This ratio compares the net sales with net working capital of the business firm. The indication given by this ratio is the number of times working capital is turned around in a particular period. The working capital turnover ratio is used to analyze the relationship between the money used to fund operations and the sales generated from these operations

WORKING CAPITAL TURNOVER RATIO =Net Sales / Net Working Capital

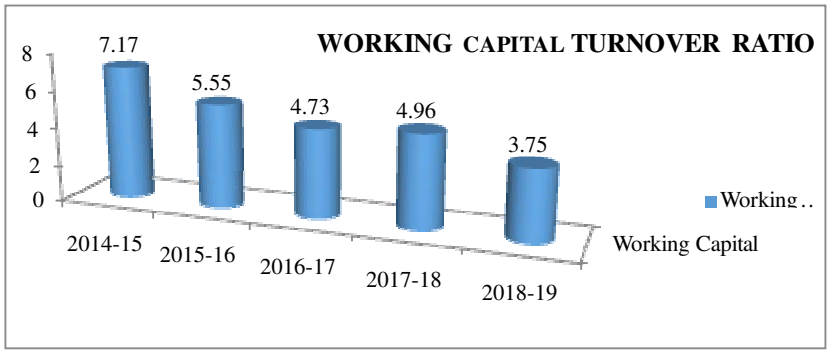
*Net Working Capital =Current Assets-Current Liabilities

Table No.6 - WORKING CAPITAL TURNOVER RATIO

Particulars	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Net sales (Rs. in lacs)	26054.80	22383.81	26073.35	29437.35	34090.63

ISSN:0971-1260
Vol-22-Issue-10-November-2019

Net working Capital (Rs. in lacs)	3634.85	4028.89	5508.30	5912.82	9081.32
Ratios	**7.17**	**5.55**	**4.73**	**4.96**	**3.75**



Graph No.5 - WORKING CAPITAL TURNOVER RATIO

INTERPRETATION:

- In a general sense, the higher the working capital turnover, the better because it means that the company is generating a lot of sales compared to the money it uses to fund the sales.
- The ratio is decreasing due to increase in amount of working capital.
- It can be seen from the graph that the company quick ratio for the year 2014-15, 2015-16, 2016-17, 2017-18 and 2018-19 were 7.17:1, 5.55:1, 4.73:1,4.96:1 and 3.75:1 respectively

INVENTORY TURNOVER RATIO:

This ratio establishes a relationship between the cost of goods sold during the given period and the average amount of inventory held in that period. The number of times the finished stock is turned over during a given accounting year. The ratio is calculated as follows:

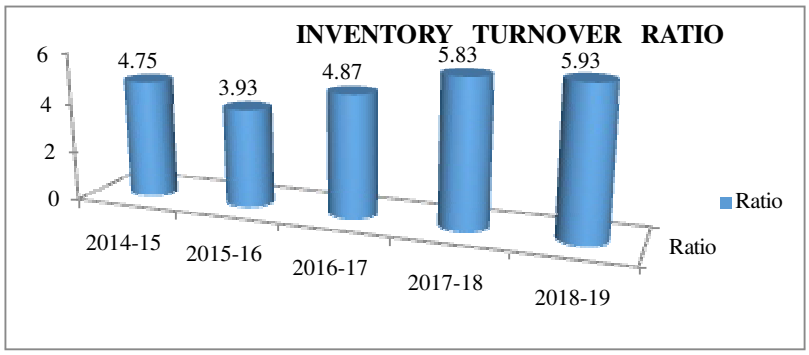
INVENTORY TURNOVER RATIO:- COST OF GOODS SOLD / AVERAGE INVENTORY

ISSN:0971-1260
Vol-22-Issue-10-November-2019

AVERAGE INVENTORY=OPENING INVENTORY + CLOSING INVENTORY /2.

Table No. 8 - Inventory Turnover Ratio

Particulars	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Cost of Goods Sold [Rs. in lacs]	14496.02	12427.19	14855.14	17602.06	22013.15
Average Inventory [Rs. in lacs]	3053.95	3160.51	3051.19	3019.26	3712.945
Ratio	**4.75**	**3.93**	**4.87**	**5.83**	**5.93**



Graph No. 7 - Inventory Turnover Ratio

INTERPRETATION:

- The higher the ratio, the better it is because it shows a rapid turnover of stock and consequently shorter holding period.
- On the other hand, if this ratio is lower, it will indicate that the slow turnover of stock and there is a longer holding period.
- As per ADOR WELDING Limitedis concerned, the inventory turnover ratio is 4.75, 3.93, 4.87, 5.83 and 5.93 for the year 2014-15, 2015-16, 2016-17, 2017-18 and 2018-19 respectively.

ISSN:0971-1260
Vol-22-Issue-10-November-2019

- The graph shows a decreasing till the year 2015-16, the reason for this may be large amount of stock has block in inventory and also due to inefficient management of inventory.
- In the year 2017-18, the ratio is increased due to strong sales and proper management of inventory which results into rapid turnover.

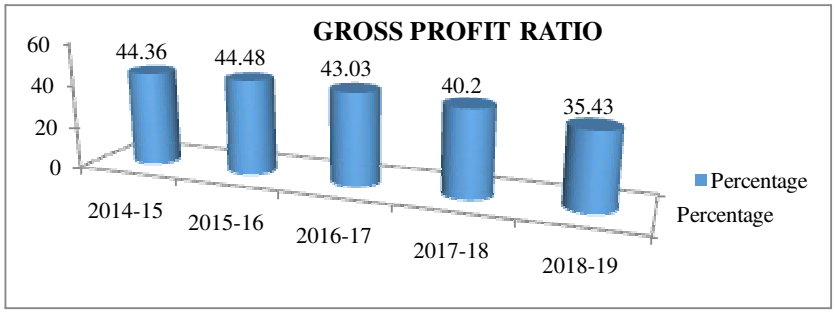
GROSS PROFIT RATIO: Gross profit ratio is the difference between the net sales [sales less sales returns] and the cost of goods sold. This ratio is calculated with the help of the following formula:

GROSS PROFIT RATIO : GROSS PROFIT / NET SALES * 100

The following data is being collected from the records of the company

Table No. 9 – Gross Profit Ratio

PARTICULARS	2014-15	2015-16	2016-17	2017-18	2018-19
GROSS PROFIT (Rs. in lacs)	11558.78	9956.62	11218.21	11835.29	12077.48
NET SALES (Rs. in lacs)	26054.80	22383.81	26073.35	29437.35	34090.63
RATIO	**44.36**	**44.48**	**43.03**	**40.2**	**35.43**



Graph No. 8 – Gross Profit Ratio

INTERPRETATION:

ISSN:0971-1260
Vol-22-Issue-10-November-2019

- This ratio shows the margin left after meeting the purchases and manufacturing cost. It measures the efficiency of production as well as pricing.
- A high gross profit ratio means a higher margin for covering other expenses like administrative, selling and distribution expenses etc i.e. other than goods sold.
- Therefore higher the ratio the better it is, it is also important for the business to maintain the ratio on the higher side, otherwise it will be difficult to cover other expenses.
- A firm can also compare its own ratio of the past with the current year's ratio to find out its performance.
- The above graph shows that the gross profit ratio of the company was 46.04%, 42.75%, 44.36%, 44.48% and 43.03% for the year 2014-15, 2015-16, 2016-17, 2017-18 & 2018-19 respectively.
- The ratio was highest in the year 2015-16 due to increase in sales as compared to last year.

NET PROFIT RATIO

The net profit ratio shows the earning left for share holders [equity and preference]. It measures the overall efficiency of all the functions of the business like production, administration , selling , financing , pricing , tax management etc. this ratio is very useful for prospective investors because it gives an overall efficiency of the firm. This ratio is calculated as follows:

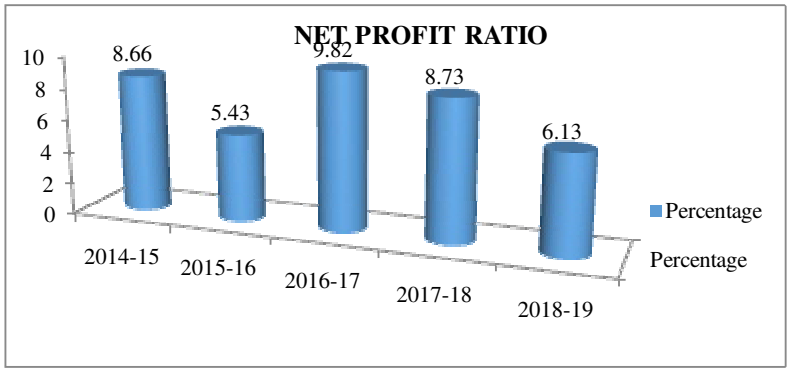
NET PROFIT RATIO : NET PROFIT / NET SALES * 100

The following data is from the records of the company:

Table No.10 – Net Profit Ratio

Particulars	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Net Profit [Rs. In lacs]	2256.01	1216.09	2559.69	2569.11	2089.11
Net Sales [Rs .in lacs]	26054.80	22383.81	26073.35	29437.35	34090.63
Ratio (%)	**8.66**	**5.43**	**9.82**	**8.73**	**6.13**

ISSN:0971-1260
Vol-22-Issue-10-November-2019



Graph No.9 – Net Profit Ratio

INTERPRETATION:

- It measures overall profitability of the business. Higher the net profit ratio higher the profit.
- It can be seen from the graph that the net profit ratio of company in year 2014-15, 2015-16, 2016-17, 2017-18 and 2018-19 was 8.66%, 5.43%, 9.82%., 8.73% and 6.13% respectively.
- There is decrease in the profit after tax from 2014-15 to 2015-16 and also form 2017-18 to 2018-19 due to decrease in profit and also there is increase in tax implication and other administrative cost.
- In the year 2014-15 profit is increased due to increase in sales.

FINDINGS:

The key findings of the project are:

- Working capital turnover ratio is continuously decreasing that shows decreasing needs of working capital.
- The debt equity ratio is NIL that means the Jyoti International Foods Pvt. Ltd. is using its owned funds for financing its requirement
- Acid test ratio is more than one but it does not mean that company has excessive liquidity.
- Debtors of the company were high; they were increasing year by year, so more funds were blocked in debtors. But now recovery is becoming faster.

ISSN:0971-1260
Vol-22-Issue-10-November-2019

- Inventory turnover ratio is improving from 2015-16 to 2018-19, which means inventory is used in better way so it is good for the company.

- The debt equity ratio is NIL that means the Jyoti International Foods Pvt. Ltd. is using its owned funds for financing its requirement.

CONCLUSION:

In the end, I can conclude that inventory is forming a major part of current assets. Working Capital is showing an increasing trend from last 5 years i.e. the need is increasing day by day. Working capital is increased as current assets are more than current liabilities. Positive working capital indicates the company has good liquidity position. Cash balance is showing an increasing trend. Company is using its owned funds for financing its requirement.

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