Chapter No. 1. Introduction

1.0. Introduction :

Sugar industry is the second largest agro-based industry in India next to textiles. India is proud of being single largest producer of cane-sugar in the world. Its share in total industrial production comes to 2.5% and provides income to 35 million farmers and their families who constitute 7.5% of rural population. There are 436 sugar factories in operation out of which state in terms of number of factories with more than 100 or so.

Sugar industry plays a vital role in the growth and development of the rural economy of Maharashtra. The Maharashtra State is one of the leading sugar producers in India. Production of sugar through co-operative processing of sugarcane was first attempted in India in 1933. There are four co-operative sugar factories in 1935. One in Uttrapradesh (Biswan) and the remaining three at Thumnapala, Etikoppaka and Vuyyu in Andrapradesh. In Maharashtra Pravara Sugar Factory at Pravaranagar (Loni) in Ahmednagar district started in 1950 is the first co-operative sugar factory founded by Padmshri Dr.Vikhe-Patil. As on 31st March, 2004 there were 178 sugar factories in Maharashtra of which 159 were in co-operative sectors, in private sector.

In Satara district having 19 co-operative sugar factories.

Ref. : Prof.S.K.Kulkarni, Co-operative Development, Phadke Prakash an2005 Oct. P.G.No.121.

1.1. Statement of the Problem :

At present, maximum co-operative sugar factories in Maharashtra are facing the problems of fixed and working Capital, Loans availiability, Sugar-cane supply and marketing etc.

This is so because if the firm can not maintain a satisfactory levelof working capital, it is likely to became insolvent and may even be forced into bankrupted.

Therefore, it become necessary to study the overall operating efficiency and particularly working capital management in co-operative sugar factories. In this study, researcher has decided to study the working capital management and it's problems.

"A STUDY OF WORKING CAPITAL MANAGEMENT OF SUGAR FACTORY WITH SPECIAL REFERENCE TO RAYAT SAHAKARI SAKHAR KARKHANA LTD., SHEWALEWADI(MASOLI), TAL-KARAD, DIST-SATARA"

1.2. Objectives of the Study :

The present study is carried out with the following objectives :

1) To study the general financial pattern of the co-operative sugar factories.
2) To study the working capital needs, sources, application and problems in this regard of co-operative sugar factories in Maharashtra.
3) To study the working and problems faced by Rayat Suhakari Sakhar Karkhana Ltd., Shewalewadi (Masoli), Tal-Karad, Dist-Satara.

4) To analyse working capital management of Rayat Sahakari Sakhar Karkhana Ltd., Shewalewadi (Masoli), Tal-Karad, Dist-Satara.

5) To present conclusions & suggestion with the study.

1.3. Scope of the Study :

This study is mainly concerned with the working capital management of Rayat Sahakari Sakhar Karkhana Ltd., Shewalewadi (Masoli), Tal-Karad, Dist-Satara for the period of five years i.e. 2001-2002, 2002-2003, 2003-2004, 2004-2005 & 2005-2006.

1.4. Research Methodology :

The required data is collected with the help of following sources :

1) Primary Data :

For collection of primary data personal interviews of the officials of the factory, officials of the financial institutions providing finance to the factory and auditors of the factory were conducted. Same type of data is collected by using observation method.

2) Secondary Data :

The study mainly relies on the secondary data collected from annual reports, manufacturing reports, financial statement etc. published by the factory from time to time. Data regarding sugar industry is collected from the data published by sugar factories federations on national and state level and other publications at national and state level of the issue.

Techniques of Analysis :

The collected data are processed & tabulated by the way of tables. At the time of analyzing the data statistical techniques such as percentages, averages etc. are used. More over technique such as 'Ratio Analysis' is applied for the analysis & interpretation.

1.5. Significance of the Study :

The issues addressed by this study are important and crucial in co-operative sugar factories. As such this study will help in improving he efficiency and overall working capital performance of sugar factories.

1.6. Chapter Scheme :

The report contains five chapter titled as :

1) Introduction
2) Financial pattern of co-operative sugar factories.
3) Profile of Rayat Sahakari Sakhar Karkhana Ltd., Shewalewadi (Masoli), Tal-Karad, Dist-Satara.
4) Analysis and Interpretation of data.
5) Conclusion and Suggestions.

Chapter No. 2. Financial pattern of co-operative sugar factories

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Financial Pattern of Co-operative Sugar Factories

General financial pattern of co-operative sugar factory involved fixed capital and working capital.

Fixed Capital :

Fixed capital means the capital which is meant for meeting the permanent or long term needs of the business. It is required for the acquisition of those assets that are used over a long period.

Generally, the fixed capital is needed for acquisition of the following assets :

a) Tangible assets such as land, building, plant & Machinery, Furniture's and fixtures, etc.

b) Intangible assets such as goodwill, patents, copy rights, promotional cost etc.

Fixed assets are necessary to run the business and hence the fixed capital is essential for investing in field assets. It can also be described as that part for total capitalization of the company which is invested in fixed assets.

In the words of Hoagland, "fixed capital is comparatively easily defined to include land, buildings, machinery and other assets having a relatively permanent existence."

Ref. : Chaudhari & Mankar, Business finance, Phadke Prakashan, 2004.

2.1.Working Capital :

The concepts of working capital is very import in every business because the term is commonly used for the capital required for day to day working. A business cannot invest whole of its capital in long term assets it may be possible the ratio of fixed capital & working capital may differ is different business depending upon its nature and volume but it is quite impossible to have no working capital to meet its day obligation. The problems involved in managing the working capital are quite different from those is managing fixed capital.

Some of the definitions of the working capital are as follows :

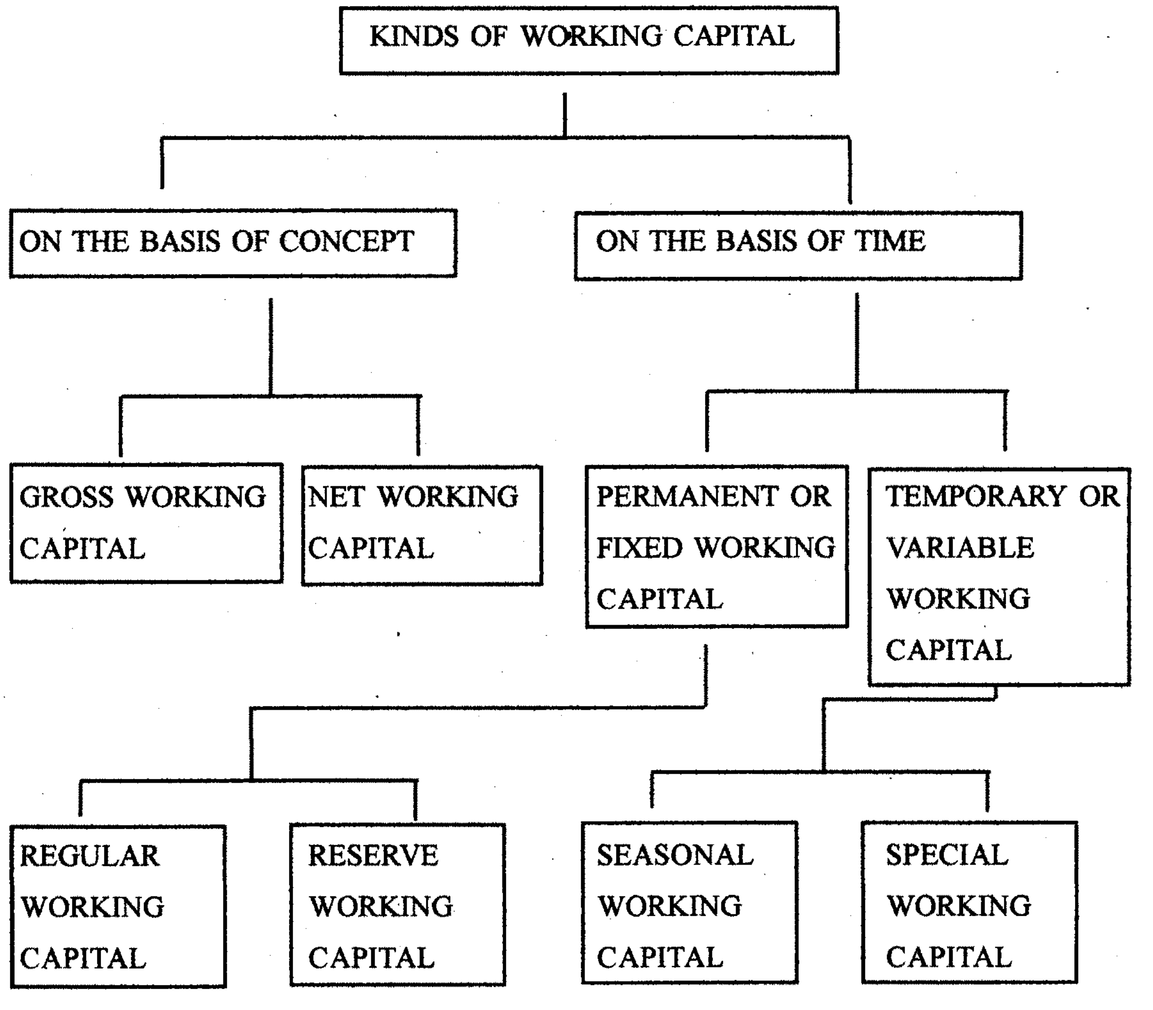
According to Hoagland, "Working capital is descriptive of that capital which is not fixed. But the more common use of the working capital is to consider it as difference between the book value of current assets and current liabilities."

In the words of shubin, "working capital is the amount of funds necessary to cover the cost of operating the enterprises."

In the words of gerestenberd, "circulating capital means current assets of the company that are changed in the ordinary course of business from one form into another, as for example, from can to inventories, inventories to receivables, receivables into cash."

Ref. : Varma & Agarwal, Fina.Mangt. King Books, 2004.

2.3. Classification or kinds of working capital :



ON THE BASIS OF TIME

1) **Temporary and variable working capital :**

Temporary or variable working capital is the amount of working capital which is required to meet the seasonal demands and some special exigencies. Variable working capital can be further classified as seasonal working capital and special working capital most of the enterprises have to provide additional working capital to meet the seasonal and special needs. The capital required to meet the seasonal needs of the enterprises is called seasonal working capital. Special working capital is that part of working capital which is required to meet special exigencies such as launching of extensive marketing campaigns for conducting research etc.

Temporary working capital differs from permanent working capital in the sense that it is required for short period and can not be permanently employed gainfully in the business.

2) **Permanent of fixed working capital :**

Permanent of fixed working capital is minimum amount which is required to ensure effective utilization or fixed facilities and for maintaining the circulation of current asset. There is always a minimum level of current assets which is continuously required by the enterprise to carry out it's normal business operations.

Ref. : Gupta & Sharma, Fin. Mangt., Kalyani Publisher-2004.

ON THE BASIS OF CONCEPT :

1) Gross working capital :

Gross working capital is equal to the value of current assets. It is the amount of funds invested in the various components of current assets. The financial managers are profoundly concerned with current assets and it enables a firm to plan and control funds to maximize to the return on investment.

2) Net Working Capital :

The net working capital is the difference between current assets and current liabilities. The concept of net working capital enables a firm to determine how much amount is left for operational requirements. Alternate definition of net working capital is that portion of current assets which is financial with long term funds.

For example, every firm has to maintain a minimum level of raw materials, work in process, finished goods and cash balance. This minimum level of current assets is called permanent or fixed working capital as this part of capital is permanently blocked in current assets. As the business grows, the requirement of permanent working capital also in case due to the increase in current assets. The permanent working capital can further be classified as regular working capital and reserve working capital required to insure circulation of current assets from cash to inventories, from inventories to receivables and from receivable to cash and so on reserve working capital is the excess amount over the requirement for regular working capital which may be provide for contingencies that may arise at stated periods such as strikes, rise in prices, depression, etc.

2.4. The Needs Objectives of working capital :

The need for working capital cannot be over emphasized. Every business needs some amount of working capital. The need for working capital arise due to the time gap between production and realization of fats cash from sales. There is an operating cycle involved in the sales and realization of cash. There are time gaps in purchase of raw materials and production, production and sales; and sales and realization of cash. Thus, working capital is needed for the following proposes :

1. For the purchase of raw materials, components and spares.
2. To pay wages and salaries.
3. To Insure day-to-day expenses and overhead cost such as fuel, power and office expenses, etc.
4. To meet the selling cost as packing, advertising etc.
5. To provide credit facilities to the customers.
6. To maintain the inventories of raw material, work in progress, stores and spares and finished stock.

2.5. Importance of working capital :

Signification of the working capital. Investment in fixed asset only is not sufficient to run the business working capital or investment in current assets how so ever small it is, is a must for the purchase of raw materials and for meeting the day to day expend hire on salaries, wages, rents, advertising etc. and for maintaining the fixed asset. Advertising etc. and for

Ref. : Gupta & Sharma, Fin.Mangt., Kalyani Publishers, 2004.

maintaining the fixed asset. Adequacy of working capital is the life blood of controlling never center of business. In adequate as well as redundant working capital is dangerous for the heat of industry. Both satiations are not warranted in a sound organizations. The advantages of working capital or adequacy working capital may be enumerated as below.

1. If proper cash balance is maintained the business can avail the advantages of cash discount by paying cash for the purchase of Raw material and merchandise.
2. It creates a feeling of security and confidence.
3. It is must for maintaining solvency and continuing production.
4. It creates sound goodwill and increases Debt capacity.
5. Easy Loans from the banks.
6. It eases distribution of dividend.
7. It helps in exploitation of good business opportunities.
8. It helps in meeting unseen contingencies.
9. It increase fixed assets efficiency.
10. The provision of adequate working capital improves the morale of the executive.
11. It helps in increasing production efficiency.

Ref. : Fin.Magt., Gupta & Sharma, Kalyani Publishers, 2004.
Fin. Magt., Varma & Agarwal, King Books, 2004.

2.6. Principles of working capital Management / Policy :

Principles of working capital Management

- Principle of Risk variation
- Principle of of cost of capital
- Principle of eauity position
- Principle of maturity of payment

1) Principle of risk variation :

Risk here reffers to the inability of a firm to meet its obligations and when they become due for payment. Larger investment in current assets with less dependance on short term borowings increases iquidity, reduce risk & there by decreases the opportenities for gain or loss on the other hand less investment in current assets with greater deperdance on short term borrowings increases risk reducess liquidity & increases profitability. In other words there is a definate inverse relationship between the degree of risk & perfitability. A concervative management prefers to minimize risk by maintaining a ligher level of current assets or working capital while a libral management assumes greater risk by reducing working capital lowever the goal of the management should be to establish a suitable treate off between pefitability are risk.

Ref. : Gupta & Sharma, Fin.Mangt., Kalyani Publishers, 2004.

2) Principle of cost of capital :

The various source of rising working capital finance have different cost of capital & the degree of risk involve generally higher the risk lower is the cost & lower the risk lower is the cost a sound working capital management should always try to active a proper balance between these to.

3) Principle of Equity Position :

This principle is concerned with planning the total investments in current assets according to this principle the amount of working capital invested in each component should be adequately justified by a firms equates position. Every rupee invested in the current assets should contribute to the net worth of the firm the level or current assets may be measured with the help of two ratio (i) current assets as a percentage of total assets & (ii) current assets a percentage of total sales. While deciding about the composition of current assets the financial manager may consider the relevant industrial averages.

4) Principle of maturity of payment :

This principle is concerned with planning the source of finance for working capital according to this principle a firm should make every effort to relate maturities of payment to its flow of internally generated foods maturity better of various current obligations is an important factor in risk assumptions & risk assessments generally shorter the maturity schedule of current liabilities in relation to expected cash in flows, the greater the inability to meet its obligation in time.

To sum of working capital management should be considered as an integral part of overall corporate management.

In the words of Louis brand, "we need to know when to look for working capital fund low to use them and low to measure plan and control them" to achieve the above maintained objectives of working capital management, the financial manager was to perform the following functions.

1) Estimating the working capital requirement.
2) Financing of working capital heeds.
3) Analysis & contrast or working capital.

2.7. Factors influencing working capital needs :

The need of working capital is not always the same it various from year to year or even month to month depending upon number of factors. There is no set rules or formulae to determine the working capital needs of the firm. Each factors has its own importance and the importance of the factors changes for a firm overtime. In order to determine the proper amount of working capital of a concern the following factors should be considered carefully.

Ref.: Varma & Agarwal, Fin.Magt., King Books, 2004.

1. Nature of Business :

The amount of working capital is basically relegated to the nature and volume of the business. In concerns, where the cost of raw materials to be used in the manufacture, of a product is very large in production to it is total cost of manufacture the requirements of working capital will be vary large

for instance, a cotton or sugar mill requires a large amount of working capital. On the contrary, concerns having large investments in fixed assets require less amount of working capital.

2. Size of Business Unit :

Size of the business unit is also a determining factors in estimating the total amount of working capital. The general principles in this regard is that the bigger the size, the larger will be the amount of working capital.

3. Terms of Purchase & Sale :

The terms on which goods are bought and sold decide to large extent, the amount of cash receive that affirm will have to hold. If affirm can manage to buy material on credit terms but sales its products on cash, it can run its operations even with a little cash balance. The reverse tendency will found where the firm makes purchases on cash basis but it has to sell its products to customers on credit terms.

4. Collection of period of receivable :

If speed of collection of accounts receivable of a firm is quick, the firm need not carry large cash balance. However, owing to liberal credit and collection policies, poor collection machinery and other factors like collection period of receivable in the firm is long, the firm will have to maintain relatively substantial reserve of cash to meet normal business expenses.

5. Credit Position :

A firm having established good image in the market circle, can carry its affairs with little cash balance. Such firm can get liberal credit facilities firm other business enterprises funds are readily available to such concerns at reasonable terms from banks & other agencies.

6. Production policy of the firm :

Production policy of the firm is an important determinant of normal cash requirements if the management of an enterprise decides to hold inventory for 3 months, production requirements to maintain fairly steady production throughout the year, it will require large amount of cash to finance the inventory requirements than the one following hand- to month policy of carrying inventory the need also depends on the kind of items manufactured the production schedule & seasonal movements.

7. Manufacturing Process :

If the manufacturing process in an industry entails a longer period because of its complex character, more working capital is required to finance that process the larger inventory is tied up in its manufacture & therefore, higher amount of working capital is needed some companies making heavy machinery & equipment minimize their investment in inventory or working capital by asking advance payment from customer as work proceeds on their orders.

Ref. : Chaudhari & Mankar, Business Finance, Phadke Praka., 2004.

8. Business Cycles :

Requirement of working capital of a company varies with cyclical variation during boom conditions, the psychology of the management is to pile up a big stock of raw material & other goods to be used in the business operations as there is an expectation to take advantage of the Lower Prices. The expansion of business units caused by inflationary conditions creates demand for more & more working capital. The other phase of business cycle, i.e., depression involved locking up of a big amount in the working capital as the inventories remain unsold & book debts cannot be recovered.

9. Turnover of circulating capital :

The speed with which the circulating capital completes its round, i.e. conversion of cash into inventory of raw material & stores, inventory of raw material into inventory of finished goods into book debts or accounts receivables, and book debts into cash accounts, plays an important & decisive role in judging the adequacy of working capital.

10. Growth & Expansion :

As company grows, it is logical to expect that larger amount of working capital will be required of course, it is difficult to draw up a proportion between the growth of the company & the growth of its working capital the growing companies require more working capital than those that are static, other things being equal.

Ref. : Gupta & Sharma, Fin.Mangt., Kalyani Publishers, 2004.

11. Dividend Policy :

A desire to maintain a specified dividend policy may affect working capital often changes in working capital bring about an adjustment of dividend policy the relationship between dividend policy & working is well established & very few companies declare a dividend without giving due consideration to their cash position. A storage of working capital acts as a check on dividend payment on the other hand a strong cash position may justify continuing dividend payment.

12. Sales Asset Relationship :

Such relationship must be minutely examined while assessing cash requirements for normal transaction purpose. A firm having larger amount of sales in relation to fixed assets will have to carry substantially large cash balance to meet inventory & receivables increased quantum of sales brings an increased cash to the firm which could be used to finance additional inventory & receivable requirements.

13. Current liabilities & Maturity Period :

A firm with large amount of current liabilities will have to hold larges cash reserve than the one with small amount of current liabilities. Furthermore, maturity period of these liabilities should also be considered while deciding the level of cash holding.

Ref. : Gupta & Sharm, Fin.Mangt., a Kalyani Publishes, 2004.

Chaudhari & Mankar, Business Finance, Phadke Prakashans, 2004.

14. Nature of Demand :

Where the demand of firm's products is highly susceptible to changer in economic conditions, the firm will have to hold large cash balance to strengthen its liquidity position this is particularly true in firms engaged in luxuries product. But the public utilities need not maintain large cash because of constant flow cash in the firm resulting from the regular demand for services.

15. Other Factors :

In addition, absence of co-ordination in production & distribution policy of the company result in high demand for working capital. Secondly, the absence of specialization in the distribution of products may enhance the need of working capital may enhance the need of working capital. Thirdly, if the means of transport & communication in the country are not well developed, the industries may face more demand for working capital. Fourthly, the import policy of the government may also affect the requirement of the working capital for the companies as they have to arrange for funds for improving goods at specified times. Lastly, the hazards & contingencies inherent in a particular type of business decide the magnitude of working capital.

Ref. : Chaudhari & Mankar, Business Finance, Phadke Prakashs, 2004.

2.8. A list of components of working capital :

A) The components of current asset are as follows :

1	Cash in hand and bank balances.
2	Bills receivables.
3	Sundry Debtors (less provision for bad debts).
4	Short term loans and advances.
5	Inventories of stocks as :
	a) Raw materials. b) Work in process c) Stores and spares d) Finished goods.
6	Temporary investments of surplus funds.
7	Prepaid Expenses.
8	Accrued Incomes.

In a narrow sense, the term working capital refers to the net working capital. Net working capital is the excess of current assets owner current liabilities, or say :

Net working capital = current assets – current liabilities.

Net working capital may be positive or negative. When the current asset exceed the current liabilities the working capital is positive and the negative working capitals results when the current liabilities are more than the current assets. Current liabilities are those liabilities which are intended to be paid in the ordinary course of business with in a short period of normally one accounting year out of the current.

Ref. : Gupta & Sharma, Fin.Mangt., Kalyani Publishers, 2004.

B) The components of current liabilities are as follows :

1	Bills payable
2	Sundry creditors or Accounts payable.
3	Accrued or outstanding expenses.
4	Short term loans, advance and deposits.
5	Dividends payable
6	Ban overdraft
7	Provision for taxation, if it does not amount to appropriation of profits.

2.9. Financing of working capital :

The working capital requirements of concern can be classified as :

a) Permanent of fixed working capital requirements.

b) Temporary or variable working capital requirements.

The various sources for the financing of working capital are as follows :

Ref. : Gupta & Sharma, Fin.Mangt., Kalyani Publishers, 2004.

Sources of working capital

Long term sources

1. Issue of shares
2. Issue of Debentures
3. Retained profits.
4. Sale of fixed assets.
5. Security from employees and from customers.
6. Term loans.

Short term sosurces

Internal

1. Depredation funds
2. Provision for taxation.
3. Accrued expenses

External

1. Trade credit
2. Credit papers
3. Bank credit
4. Customers credit
5. Public deposits
6. Loan from managing director or direcdtors
7. Government assistance.

1. Issue of shares :

It is the most important source of long term regular working capital. As far as possible, efforts should be made to procure the maximum amount of regular working capital out of proceed of issue of shares it creats no burden or the fixed charge on the earning assets of the company. Morever, the company is not under obligation to return the capital.

2. Issue of Debentures :

Regular working capital can also be procered by issue of debentures or bonds the cost of capital is lower in this case. Byi issuing debentures, company mayi trade on equity in favourable circumstances but it is must be cautious raising funds by issuing debentures if there is no stability in the arning of the firm because they create charge on the earning assets of the company.

Ref. : Gupta & Sharma,Fin.Mangt., Kalyani Publishers, 2004.
Varma & Agarwal, Fin.Mangt., King Books, 2004.

3. Retained Profits :

Accumulated large profit is also considered to be a good source of financing long turn working capital requirements. It is the best and the cheapest source of finance. It creates no charge on future profits, a part of earned profits are ploughed back by the firms in meeting the working capital requirements by the firm in meeting the working capital requirements.

4. Sale of fixed assets :

If there is any idle asset in the firm, it can be sold out and proceeds may be utilized for financing the working capital requirements.

5. Security from employees and from customers :

Certain companies require a security deposits from there employee before giving them employment under the terms of service contract similarly public utility concerns e.g. electricity distribution co or cooking gas supply companies require security deposits for there registered customer.

6. Term Loans :

Mid term and long term loans for a period above 3 years provide important sources of working capital. Such term loan can be borrowed from the special financial institution such as is the industrial development in Bank of India. The industrials finance corporation, the life insurance corporation and commercial bank etc.

Ref. : Varma & Agrawal, Fin.Mangt., King Books, 2004.

Gupta & Sharma, Fin.Mangt., Kalyani Publishers, 2004.

Sources of short term working capital :

I) Internal Sources :

1) Depreciation Funds : Depredation funds created out of profit of the company provide a good sources of working capital provided they are not invested in or represented by an assets.
2) Provision for Taxation : There remains a time lag between the making the provision for and payment of taxation. A company may utilize such provision during the intermittent period of temporarily.
3) Accrued Expenses : The company some time post phone the payment cretin expenditure due on the date of finalization of the accounts.

II) External Sources :

1) Normal trade credit : Trade creditors provide short term finance to the company by selling the goods inventories and equipments on the basis of deferred payment.
2) Credit Papers : Under this category, bills payable promises note etc. are included he acceptor of a bill of exchange gets time in making payment for loan. It is like a credit extended to him by the creditor against his acceptance.
3) Bank Credit : The greater part of working capital is supplied by commercial bank to there customers through direct advances in the safe of loans, cash credit or overdraft and through discounting the credit papers e.g. B/R., P/N etc.

Ref. : Gupta & Sharma, Fin.Mangt., Kalyani Publishers, 2004.

4) Customers Credit : Advances may also be obtained from customers against the contract a entered into by the enterprise. The amount can be used for purchasing raw materials, paying wages and so on.

5) Public Deposits : Most of companies in recent years depend on this source to meet their working capital requirements. It had been most common in cotton textile mills in Bombay and Ahmedabad bout now almost every public limited company rises finance from this sours ranging from 6 month to 2 years to meet working capital needs.

6. Loans from managing directors or directors : Some times director or managing director of the company provide loans the company every negligible rate of interest or at no rate of interest.

7. Government Assistance : Central and state Government of the country provide short turn finance to industries or business by allowing them tax concessions, sanctioning direct loans or grants to industries or a class of industries to assist their production programmers etc.

Ref. : Gupta & Sharma, Fin.Mangt., Kalyani Publishers, 2004.