CHAPTER V

PRESENTATION, ANALYSIS AND INTERPRETATION

5:1 Working Capital Position.

5:2 Liquidity Position.

5:3 Long Term Solvency.

5:4 Profitability.

CHAPTER V

PRESTENTATION, ANALYSIS AND INTERPRETATION

5:1 WORKING CAPITAL POSITION :

The total capital required by any concerned is grouped under, Fixed Capital and Working Capital. Fixed Capital, so called long term capital is generally blocked permonently in the investment of fixed assets. And working capital is needed for the investment in current assets. The sum total of investment in current assets is called gross working capital and current assets minus current liabilities is known as net working capital. The success of evry business depends upon maintainence of saund working capital. The smooth and steady operating of working capital cycle is must for the growth and development of any business concern.

The working capital position of this mill is studied by following the net working capital concept. The analysis of the data given in the following tables will give an idea about the working capital position during the study period.

The table No.5:1 clearly shows that every year current assets are more than current liabilities. This also shows that the mill has maintained the favourable working capital in all the years of study

TABLE No. 5:1

POSITION OF WORKING CAPITAL PERIOD 1988 to 1992

PARTICULARS	1988 Rs.	1989 Rs.	1990 Rs.	1991 Rs.	1992 Rs.
Current Assets	6,07,52,662.00	5,03,19,014.00	6,52,78,397.00	8,06,26,032.00	9,81,11,658.00
Current Liabilities	2,17,34,114.00	2,59,44,497.00	3,76,46,100.00	2,09,93,257.00	3,69,74,638.00
Working Capital	3,90,18,548.00	2,43,74,517.00	2,76,32,297.00	5,96,32,775.00	6,11,37,020.00

C.A Includes :- Cash in Hand, Cash at Bank, Debtors, B/R., C/A.

C.L. includes :- Creditors, o/s.Exp., B/P., Expend.Occrued, C/L.

TABLE NO. 5:2

CHANGES IN WORKING CAPITAL

YEAR	WORKING CAPITAL Rs.	INCREASE Rs.	DECREASE Rs.
1988	3,90,18,548.00	---	
1989	2,43,74,517.00	---	1,46,44,029.00
1990	2,76,32,297.00	32,57,780.00	---
1991	5,96,32,775.00	3,20,00,478.00	---
1992	6,11,37,020.00	15,04,245.00	---

period. The exact increase or decrease as compared to previous year is shown in the table No.5:2

The data in the table No. shows that working capital is increased from Rs.390,18,548/- in 1988 to Rs.611,37,020/- at the end of 1992. It is also deal from the said table that only in the year 1989 there was a decrease in the working capital. In rest of the years the mill has maintained the increasing trend of working capital. The reasons for such increase or decrease in working capital can be studied from the data given in the table No.

In the table No.5:3 it is seen that working capital was increased to Rs.1.02 crores in the year 1988-89 because -

(1) An increase in current assets.
(2) Decrease in current liabilities.

In the table No.5:4 shows decrease in working capital of Rs. 1.37 crores. This is because -

(1) Increase in inventory (Current Assets), loans and advances, sundry creditors.
(2) Decrease in Sundry Debtors and cash and bank balance and other liabilities.

TABLE No.5:3

STATEMENT OF CHANGES IN WORKING CAPITAL : 1988 - 1989

(Rs. in Crores)

PARTICULARS	1988	1989	Increase	Decrease
(A) CURRENT ASSETS :				
Inventories				
Sundry Debtors				
Cash & Bank Balance	6.75	5.31	--	1.44
Loans & Advances				
Total 'A'	6.75	5.31		
(B) CURRENT LIABILITIES :				
Sundry Creditors				
Provisions	2.17	2.59	0.42	--
Total 'B'	2.17	2.59		
NET WORKING CAPITAL (A - B)	(4.58)	(2.72)		
Increase in Working Capital	1.02	--	1.02	--
	(2.72)	(2.72)	1.44	1.44

Figures in bracket shows positive balances.

TABLE No. 5:4

CHANGES IN WORKING CAPITAL

(Rs. in Crores)

PARTICULARS	1989	1990	Increase	Decrease
(A) CURRENT ASSETS :				
Inventories	2.38	1.14	---	1.24
Sundry Debtors	2.00	3.17	1.17	--
Cash & Bank Bal.	0.06	0.13	0.07	--
Loan & Advances	0.74	0.70	--	0.04
Total C.A.(A)	4.18	4.14		
Sundry Liability				
Sundry Creditors	2.13	3.48	--	1.35
Provision	0.08	0.06	0.02	--
Total C.L. (B)	2.21	3.54		
Net Working Capital (A - B)	(1.97)	(0.60)	1.37	
Decrease in W.Capital		1.37		
	1.97	1.97	2.63	2.63

NOTE : Figures in bracket show/s positive balances.

TABLE No 5:5

CHANGES IN WORKING CAPITAL

(Rs. in crores)

PARTICULARS	1990	1991	Increase	Decrease
CURRENT ASSETS :				
Inventories	2.38	3.46	1.08	
Sundry Debtors	3.17	2.72	--	0.45
Cash & Bank Bal.	0.13	0.11	--	0.02
Loan & Advances	0.70	1.49	0.79	--
total C.A.(A)..	6.38	7.78		
CURRENT LIABILITES :				
Sundry Crediots	2.13	1.52	0.61	
Provisions (Other Liabilities)	0.08	0.52	--	0.44
Total C.L. (B)	2.21	2.04		
Net Working Capital (A - B)	(4.17)	(5.74)	--	1.57
Increase in Working capital	1.57			
	5.74	5.74	2.48	2.48

Note : Figures in bracket shows positive balances.

The reasons for increase in working capital in 1991 are :

(1) Decrease in sundru debtors and also decrease in other liabilities.

(2) Increase in inventories and loans & advances.

TABLE No. 5:6

CHANGES IN WORKING CAPITAL

(Rs. in Crores)

PARTICULARS	1991	1992	Increase	Decrease
CURRENT ASSETS :				
Inventories	3.46	4.86	1.40	--
Sundry Debtors	2.72	3.06	0.34	
Cash & Bank Bal.	0.11	0.47	0.36	
Loan & Advance	1.49	1.11	--	0.38
Total C.A.(A)..	7.78	9.50		
CURRENT LIABILITIES :				
Creditors	1.52	3.47	--	1.95
Other Liabilities (Provisions)	0.52	0.14	0.38	
Total C.L. (B)	2.04	3.61		
Net Working Capital (A - B)	(5.74)	(5.89)		0.15
Increase in W.Capital	0.15			
	5.89	5.89	2.48	2.48

Note : Fiqures in bracket show positive figuires.

The net increase in working capital is due to :

(1) Increase in sundry debtors, inventories, cash and bank balances and creditors.

(2) Decrease in loans & advances and other liabilities.

5: 2 LIQUIDITY RATIOS :

(1) CURRENT RATIO :

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilites}}$$

TABLE No.5:7

PARTICULARS	1988	1989	1990	1991	1992
Current Assets	60752662	50319014	65278397	80626032	98111658
Current Liability	21734114	25944491	37646100	20993257	36974638
	3.09 : 1	2.22 : 1	1.96 : 1	4.26 : 1	2.89 : 1

INTERPRETATION :

That inventories constitute the major portion of the current assets of the Gadag Co-operative Textile Mill Ltd., Hulkoti. As such, the rule of thumb is that the current assets should not be less than twice the current liabilities applied fully. During the period of study from 1988 and 1992, the current ratio varied from 3.09 : 1 times to 2.89 : 1 times. It was less than two times in 1990. It was more than two times indicating a very satisfactory

short term financial strength in these four years.

The ratio being so high as 4.26 : 1 times in 1991. This was due to accumulation of heavy inventories and cash credit loans were not taken by the mill. Besides these the expenditure was managed by the mill with its own resource.

In the year 1990 the current ratio is less than two i.e. 1.96 : 1 and there was large capital locked in the form of inventories. Therefore, the short term financial position was doubtful.

Co. having a sound short term solvency accept in the year 1990.

(2) QUICK RATIO :

TABLE No.5:8

YEARS ..	1988	1989	1990	1991	1992
Ratio	1.02 : 1	2.08 : 1	1.70 : 1	3.44 : 1	2.21 : 1

INTERPRETATION :

This is the true test of going convern solvency of a business. As general sale, when the current assets equals or exceeds the current liabilities, the

financial position may be considered satisfactory.

Under the study seems to be quite satisfactory. The ratio was obiously more than one in the year 1988, 1990 in 1989, 1991, 1992. The quick ratio 2.08 : 1 3.44 : 1 and 2.21 : 1 due to considerable increase in sundery debtors and loan and advances and decrease in current liabilities excess liquidity an a sound liquidity position.

Thus it is clear that relationship between liquid assets and liquid liabilities is sound during all the five years.

$$\text{Quick ratio} = \frac{\text{Current Asset - Stock}}{\text{Liability}}$$

These quick assets consist of the following :

1) Cash in hand, Bank and Postal Savings.

2) Loan and advances, and

3) All receivable.

That is excluding stock of inventories crop in progress and prepaid expenses all current assets have been taken as quick assets.

Current Liabilities includes :

1) Recoveries payables.

2) Other dues payable, and

3) Other liabilities such as provision for taxation.

5:3 LONG TERM SOLVENCY :

Bankers and other short term creditors are more interested in current debts paying ability of a business i.e. short term solvency of the business concern. While shareholders and other financial institutions which provide long term finance are mainly concerned with the long term financial prospects of the business. Hence, analysis and interpretation of long term solvency of the business is significant from view point of shareholders and financial institution.

Long term solvency means the obility of a business concern to meet its long term obligations. It implies that business concern must have an ability to discharge its liabilities through the realisation of its assets. To achive this long term solvency proper balance between assets and liabilities should be maintained.

Analysis of long term solvency help the shareholders bankers and prospective investors in taking decisions on selling or rataining ownership rights, granting or otherwise long term credit and making investment in the concern.

Ratios applied to be judge long term solvency Various ratios are applied to judge the long term solvency few of them are -

1) Debt Equity Ratio :-

This ratio express a relationship between total liabilities (external equities) and the owner's equity (Internal equities). This ratio is also known as external internal equity ratio.

Formulation :

$$\text{Debt Equity Ratio} = \frac{\text{Liabilities}}{\text{Owner's Equities}}$$

OR

$$\frac{\text{Outsider's Funds}}{\text{Shareholder's Funds}}$$

* Outsiders Fund consists of loan for working capital, secured secured loan, unsecured loan, deposits and current liabilities and provision.

* Shareholders fund consists of share capital and reserves and surplus (Share capital + calledup share + Share Ammant + General Reserve + Other Capital + Subsidy)

TABLE No.5:9

DEBT EQUITY RATIO (1988 to 1992)

Particulars	1988	1989	1990	1991	1992
Outsiders Fund	6,03,49,973.09	4,26,35,940.52	5,49,45,332.88	4,88,51,421.70	7,63,75,132.68
Shareholder Fund	2,77,32,342.75	5,81,89,491.54	1,64,52,963.78	10,00,29,050.00	10,62,78,950.00
	2.17 : 6	0.73 : 2	3.33 : 9	0.48 : 8	0.71 : 8

INTERPRETATION :

As this ratio expresses the relationship between external equity and internal equity. The standard ratio is 1 : 1 i.e. shareholder's funds must be equal to long term liabilities.

As compared to standard ratio this ratio's are not good, and it is generally below than standard ratios.

In the year 1988 it is to 2:17:1 this increase in the debt equity ratio was due to substantial in the borrowed funds. In the year 1989 it can be seen that the ratio was below the generally accepted norm 1 : 1 However in the year 1990 'Co' has managed to increase this ratio upto 3.33 : 9 by decreasing borrowed capital and again in the year 1991 to 1992 below the norm 1 : 1. It shows decreasing of debt which is not managable limit of the 'Co'.

(2) RATIO OF FIXED ASSET TO PROPREITOR's FUND :

This ratio indicates the relationship between the ownership funds (shareholder's funds or proprietors funds) and fixed assets. When the amount of proprietor's funds exceeds the value of fixed asset, a part of the Net Working Capital is supplied by the shareholder's provided that there are no other

non-current assets, and when proprietors funds are less than the fixed assets, and creditor's obligations have been used to finance a part of the fixed assets.

This ratio is worked out as under :

$$\frac{\text{Book value of fixed assets}}{\text{Proprietor's funds}}$$

For calculating this ratio of the factory fixed assets consist the fixed assets which are shown in the balance sheet.

Proprietor's funds includes share capital plus all reserves and surplus. The trend of this ratio is as follow.

TABLE No.5:10

RATIO OF FIXED ASSETS TO PROPRIETOR'S FUNDS

Year	Amount	Ratio
1988	384,78,340.00 / 277,32,342.00	1.39
1989	385,23,033.00 / 581,89,491.00	6.62
1990	436,48,278.00 / 164,52,963.00	2.65
1991	477,26,931.00 / 1000,29,050.00	0.48
1992	722,25,737.00 / 1062,78,950.00	0.68

INTERPRETATION :

This ratio shows the extent of proprietors funds invested in fixed assets.

The standard ratio for industrial undertaking is 65 : 1.

The trend of this ratio fluctuates during the period of study from 1.39 in 1988 to 1989 6.62, 1990 2.65, 1991 0.48, 1992 0.68. There is more investment of shareholders fund in fixed assets and this is not an ideal policy of investment. When there is excess investment in fixed assets the part of working capital has to supply by the shareholders.

This ratio has declined to 0.48 in 1991, 0.68 in 1992, so accepted standard ratio of both. It is so difficult to comment directly because business has its own policy about investment in current assets and in fixed assets one way there shareholder's fund show decreasing trend because of decreasing in reserves and surplus.

(3) RATIO OF CURRENT ASSETS TO PROPRIETORS FUNDS :

This artio shows precentage of shareholder's funds invested in current assets. This ratio should be used in conjunction with a ratio of fixed assets to proprietors funds. It ratio of current assets to proprietors funds is higher than that fixed assets to proprietors funds, it is an indication of the financial strength of the business.

This ratio is calculated by the following formula :-

$$\frac{\text{Current Assets}}{\text{Proprietor's Funds}}$$

For Calculation of this ratio current assets include -

i) Cash and Bank Balance.

ii) Loans and Advances.

iii) Stock.

iv) Prepaid expenses.

Proprietor's fund includes share capital plus all reserves and surplus.

TABLE No.5:11

RATIO OF CURRENT ASSETS TO PROPRIETORS FUND

YEAR	AMOUNT	RATIO
1988	6,07,52,662.00 / 2,77,32,342.00	2.19
1989	5,03,19,014.00 / 5,81,89,491.00	0.86
1990	6,52,78,397.00 / 1,64,52,963.00	3.97
1991	8,06,26,032.00 / 10,00,29,050.00	0.80
1992	9,81,11,658.00 / 10,62,78,950.00	0.92

INTERPRETATION :

There is no standard for comparison of this ratio in the year 1988 2.19 portion of the

proprietor's funds used in current assets. In the year 1989 this portion decreased to 0.86 and it increased n the year 1990 to 3.97

Since the investement in current assets in all five years is more than shareholder's fund. It indicates that outsider's funds in large extent have been invested in current assets.

As this ratio is lower than the ratio of fixed assets to proprietors funds, it is an indication of financial weakness.

Only in the year 1990 this ratio is higher than fixed assets to proprietors fund, and that year only the financial position of the factory is in not so good condition.

(4) RATIO OF FIXED ASSETS TO FIXED LIABILITIES :

This ratio is useful to findout long term solvency. This ratio is calculated whether the fixed assets are sufficient to meet the fixed liabilities if the firm goes into liquidation.

$$\frac{\text{Fixed Assets}}{\text{Fixed Liabilities}}$$

TABLE No. 5:12

RATIO OF FIXED ASSETS TO FIXED LIABILITIES

Year	amount	Ratio
1988	370,34,261 / 358,07,236	1.03
1989	371,66,067 / 191,88,790	1.94
1990	416,26,749 / 152,28,928	2.73
1991	447,63,363 / 278,58,164	1.61
1992	677,72,360 / 394,00,494	1.72

For calculation of this ratio fixed liabilities are taken as -

i) Loan

ii) Deposits from NRD and all other Deposits

INTERPRETATION :

On an average this ratio is 1.81 during the period of study. Low ratio indicates financial weakness in terms of long term obligation. Such situation my create bad impression among the shareholders about safty of their funds.

In the year 1988 and 1989 this ratio remained tthe same and the year 1989 it increased to 1.94.

For the last two years the ratio is near to equal. But it is in an increasing order for these two years. And much satisfactory than preceeding years.

This ratio is lower than standard ratio because of faster increase in long term liabilities. It signifies unsatisfactory postion to meet its long term obligations.

In the year 1991-92 additional loan has taken for establishement of from I.D.B. (Syndicate Bank) N.C.D.C. That is whay this ratio declined in that year.

5:4 PROFITABILITY RATIO :

GROSS PROFIT MARGIN :

The first profitability ratio in relation to sales is the gross profit margin. It is calculated by dividing the gross profit by sales. The gross profit margin is calculated by following formula :

$$\text{Gross Profit Margin} = \frac{\text{Gross Profit}}{\text{Sales}} \times 100$$

For the Gadag Co-operative Textile Mill Ltd., Hulkoti, the gorss profit margin for the following five years is calculated by following table.

TABLE NO.5:13

RATIO OF GROSS PROFIT TO SALES OVER VARIOUS YEARS

Years	Sales	Gross Profit	Gross Profit Margin
1988	8,03,60,295.15	5,95,939.66	0.74%
1989	10,53,08,804.67	1,26,16,776.48	11.98%
1990	8,07,43,740.18	1,92,36,073.00	23.82%
1991	11,73,19,961.51	2,34,17,561.11	19.96%
1992	13,44,67,240.92	2,43,63,040.89	18.19%

It can be noted from above table that the Mill's gross margin in the year 1988 was 0.74% an it increased up to 11.98% in the year 1989 because Mill sale has gone up. In the year 1990 it increase upto 23.82% because of increase in profits, sales has gone up due to the production of higher grade of yarn and manufacturing expenses proportionately decreased as compare to the previous year. But in 1991 it again slumped down to 19.96% which shows that the firm earned only Rs. 19.06 on sale of Rs. 100/-. Further in 1992 the company earn Rs. 18.19 on per hundred rupees worth of sale.

NET PROFIT MARGIN :

A reasonable gross profit margin is necessary to earn adequate net profits. Net profit is obtained when operating expenses and income tax are subtracted from the gross profit. The net profit margin ratio is measured by dividing net profit after tax by sales.

$$\text{Net Profit Margin} = \frac{\text{Net Profit After Tax}}{\text{Sales}} \times 100$$

For the Gadag Co-operative Textile Mill Ltd., Hulkoti, the net profit margin after tax

calculating in the following table.

TABLE No.5:14

RATIO OF NET PROFIT AFTER TAX TO SALES OVER VARIOUS YEAR

YEAR	SALES	NET PROFIT	NET PROFIT MARGIN
1988	8,03,60,295.15	2,75,463.84	0.34%
1989	10,53,08,804.67	38,73,557.85	3.68%
1990	8,07,43,740.18	93,39,560.29	11.57%
1991	11,73,19,961.51	99,11,528.85	8.45%
1992	13,44,67,240.92	92,56,834.12	6.88%

The foregoing table indicates that the rate of profits to total sales in 1988 was 0.34% which mounted up to 3.68% in. But in 1990 it was jumped to 11.57% which shows that the firm earned Rs. 11.57 on sales of Rs. 100. Further in 1991 the Mill earned only 8.45%. Thus it earned only Rs. 8.45 on per hundred rupees worth of sales and further 1992 earned Rs.6.88 on per 100/- rupees worth of sales.

OPERATING RATIO :-

The operating ratio is an important ratio that explains the change in the net profit margin ratio. This ratio is computed by dividing alll operating expenses - cost of goods sold, selling

expenses and general and administration expenses by sales.

$$\text{Operating Ratio} = \frac{\text{Cost of Goods Sold} + \text{Operating Expenses}}{\text{Sales}} \times 100$$

The operating ratio is a yardstick of operating efficiency. The operating ratio indicates the average aggregative variation in expenses where some of may be increase, while some may be falling.

A higher operating ratio is unfavourable since it will leave a small amount of operating income to meet interest, dividends etc. Certain expenses are within the managerial discretion, therefore, it should be seen whether change in expenses is due to change in the management policy detailed analysis may be revel that the year to year variations in the operating ratio are temporary in nature arising due to some temporary conditions. The variations in the operating ratio, temporary or long lived, can occure due to several factors such as -

a) Changes in the sales prices,

b) Changes in the dividend for the product

c) Changes in the cost of goods sold and operating expenses.

d) Changes in the proportionate share of sales of different product with varying gross margins.

These and other causes of variation in the operating ratio should be throughly examined.

To get a comprehensive idea of the behaviour of operating expenses, variation in the ratios over a number of years we should be studied here for Gadag Co-operative Textile Mill Ltd. (Hulkoti). The Operating ratio are follows over various years. Here the operating ratio is -

$$\frac{\text{Manufacturing Expenses + Depreciation}}{\text{Sales}} \times 100$$

TABLE No.5:15

RATIO OF OPERATING EXPENSES TO SALES OVER VARIOUS YEARS

Year	Sales	Operating Expenses	Operating Ratio
1988	8,03,60,295.15	7,77,43,690.00	96.74%
1989	10,53,08,804.67	9,13,58,678.00	86.75%
1990	8,07,43,740.18	7,41,02,175.00	91.77%
1991	11,73,19,961.51	10,43,36,266.00	88.93%
1992	13,44,67,240.92	12,72,36,106.00	94.62%

The forgoing table clearly states that the operating expenses to sales is prominantly responsible for fluctuations in proritability.

In the year 1988 the operating ratio is 96.74% and it has been come down in the year 1989 to 86.75% so the operating ratio decreased by 9.99%. It shows management efficiency and the policies adopted by management were favourable as compared to the previous year. In the year 1990 it was again increased by 5.02%. In the year 1991 it was again decreased by 2.84%. In the year 1992 it was increased by 5.69% that the Mill incurred operating expenditure Rs.94.62 on sales of Rs. 100/-. and left very small amount of margin (Rs. 5.4).

RETURN ON INVESTMENT (ROI) :

The profitability of the firm is also measured in relation to investment. The term investment may refer to total assets, capital employed or the owner's equity. Accordingly may profitability ratio's in relation to investment can be calculated the important ratio's discussed below :

1) Return on Assets (ROA).
2) Return on Capital Employed (ROCE)
3) Return of Shareholders Fund (ROSF)

1) RETURN ON ASSETS :

The return on assets or profit to assets ratio is net profit after tax divided by total assets.

$$\text{Return on Assets} = \frac{\text{Net Profit after tax}}{\text{Total Assets}}$$

Note : Here the total assets means Fixed Assets + Current Assets.

For the Gadag Co-operating Textil Mill Ltd., Hulkoti, return on assets ratio are following over various year's.

TABLE No.5:16

RETURN ON ASSETS OVER VARIOUS YEAR

YEAR	TOTAL ASSETS	NET PROFIT AFTER TAX	RETURN ON ASSET
1988	10,42,99,674.00	2,75,463.00	0.26%
1989	9,47,75,832.00	38,73,557.00	4.08%
1990	11,53,43,646.00	93,39,560.00	8.09%
1991	13,43,55,945.00	99,11,528.00	7.38%
1992	17,49,69,069.00	92,56,834.00	5.29%

(Net Fixed Asset = Asset - Dep. + CA + Inv.)

The above table shows that the ratio shows rather favourable position upto 1990 and thereafter

the ratio started declining in 1990, the Mill could earn maximum return on assets.

TABLE No.5:17

RETURN ON SHAREHOLDER'S EQUITY

Years	Shareholders' Equity	Net Profit after tax	Return on Shareholders Equity
1988	2,77,32,342.00	2,75,463.00	0.99%
1989	5,81,89,491.00	38,73,557.00	6.66%
1990	1,64,52,963.00	93,39,560.00	56.76%
1991	10,00,29,050.00	99,11,528.00	9.90%
1992	10,62,78,950.00	92,56,834.00	8.71%

The data in the above table shows that he Mill has made the highest raturn on equity capital in the year 1990 (i.e. 56%). Then the return started declining year after and reached to 8.7% in 1992. It was mainly because of increase in the investment of fixed assets though there was no serious decline in the net profits.