CHAPTER VI

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The Gadag Co-operative Textile Mill Ltd., Hulkoti, Gadag Taluka, (Karnataka) recognises as one of the well established and developed textile mills in Karnataka State. It was registered on 17th January,1981 in the rural and backward area of Dharwad District.

Research of this mill has been undertaken with a view to examine and analyise its solvency, liquidity and profitability position with the help of "Ratio Analysis". After close scrutiny of the study the following conclusions are drawn which includes both the findings and suggestions. These findings and suggestions are divided in to following parts.

1) From working capital positon.
2) From the view point of short term solvency.
3) From the view point of long term solvency.
4) From the view point of profitability.

(1) WORKING CAPITAL POSITION :

The success of every business depends upon maintainence of sound working capital. The smooth operation of working capital cycle is a must for the growth and development of any business concern.

The working capital position of this mill is studied for the period 1988 to 1992. It clearly shows that every year current assets are more than current liabilities. Thus the mill has maintained a favourable working capital in all these years of study period.

(2) LIQUIDITY POSITION :

Short term solvency means ability of the firm to meet its current obligation without loss.

This solvency position is examined with following ratios.

(i) Current Ratio :

The current ratio of the mill in all the year is more than standard requirement which is 2:1 except in the year 1990 (1.96).

During the period of study, the ratio varied from 3.09 times in 1988 to 2.89 times in 1992, indicating a very much satisfactory, short term financial strength fo the mill and heavily accumulated inventories without cash credit has holped the mill to maintain the favourable working capital.

Too high or too low ratio is not good from the new point of optimum utilisation of assets.

Therefore the mill must give attention towards the proper investment in current assets.

(ii) Quick or Liquidity Ratio :

This is the true test of solvency position of a business. As a general rule if current assets are equal or exceed the current liabilities the financial position may be considered satisfactory.

The liquidity position of the mill was sound during the period under study from 1988 to 1992. This ratio varied from 1.02 : 1 times in 1988, 2.08 : 1 times in 1989, 1.70 : 1 times in 1990, 3.44 : 1 times in 1991 and 2.21 : 1 times in 1992, thus it is more than the generally accepted norm and indicates a sound short term financiall strength.

In the year's 1989, 1991, 1992 the liquidity position was so good as compared to the ratio in 1988 and 1990.

The reason for decreasing (1988, 1990) this ratio is increase in current liabilities.

Therefore it is necessary to maintain the porper balance between liquid assets and current liabilities. Therefore the mill should watch to maintain this position in the future period also.

(3) LONG TERM SOLOVENCY :

Long term solvency means ability of the concern to meet its long term obligations without loss.

This can be tested with various devices.

(i) Debt Equity Ratio :-

As compared to standard ratio this ratios is not good. It is below the standard ratio, but in the year 1988 it maintained 2.17 : 1. This increase in the debt equity ratio was due to substantial increase in borrowed funds. In the year 1989 it can be seen that the ratio was below the generally accepted norm 1 : 1. In the year 1990 mill has managed to increase position ratio up to 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, this relationship between external equity and internal equity is not favourable.

Mill has to keep close watch to maintain standard position in future period.

(ii) Fixed Assets to Proprietors Funds Ratio

The trend of this ratio shows the fluctuations during the period of study i.e. 1.39 in

1988, 6.62 in 1989, 2.65 in 1990, 0.48 in 1991, 0.68 in 1992 i.e. ratio's are more than generally acceptable norm except in the years 1991, 1992.

Where there is excess investment in fixed assets the part of working capital has to be supplied by the shareholders.

This investment policy is not ideal but it is not favourable to comment directly because every business has its own policy, so mill should give due consideration to its investment policy and /use the shareholders funds in proper way.

(iii) Current Assets to Proprietors Funds

In the year 1988 (2.97) and 1990 (3.97) the ratios are higher than fixed assets to proprietors fund and shows that the financial position of the mill is not so favourable.

Similarly during all period of study, investment in current assets less than proprietors funds. It indicates that outsider's funds have not been invested in current assets in large extent.

This policy of investment is ideal, thus management must try to maintain this ratio at the normal expected level in future period.

(iv) Ratio of Fixed Assets to Fixed Liabilities :-

On an average this ratio is 1.81 during the period of study. Low ratio indicates financial weakness in terms of long term obligations. Such a situation may create bad impression in the minds of shareholders about the safety of their funds. Hence this ratio should be satisfactory. In the last two years the ratio was to some extent ideal. So in order to meet long term obligations without loss or distrubance factory should keep close watch to maintain this ratio at the expected standard level.

(4) PROFITABILITY POSITION :-

(i) Gross Profit to Net Sales :

During the period of study this ratio was on an average of 14.94%. Though sales was in increasing trend but there was no corresponding increase in gross profit. It was due to increase in manufacturing expenses and excess stock of inventories.

There is scope to control manufacturing expenses. Therefore management should take the necessary action to bring down such expenses and must try to raise this ratio so that maximum portion of gross profit will be available to absorb non-operating expenses.

(ii) Net Profit to Net Sales :

Considering this ratio as the profitability position of the mill was not so good. This was only because of high rate of interest on loan in 1988 which increased moderately upto the year 1992. Similarly there was an increase in administrative and other expenses. It means that all the portion of gross profit was absorbed by adminstrative expenses general expenses, interest and depreciation. To have sufficient margin of net profit, there should be control over expenses particularly adminstrative, general expenses and other variable expenses.

(iii) Operating Ratio :

The operating ratio is a yard stick of operating efficiency.

The operating ratio indicates the average aggregate variation in expenses where some of them may be increasing while some may be falling.

During the period of study it is clearly seen that, the operating expenses to sales, is prominantly responsible for fluctuations in profitability.

During the year 1988 to 1992 there was higher operating ratio which was unfavourable to the Mill, therefore it is suggested that the Mill should try its best to manage the operating expenses within the limit and accordingly the management should control the administrative expenses which formed the major part of the total operating expenses.