A Study on relationship between Long term finance and Working Capital in Manufacturing Sector

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ABSTRACT

Manufacturing consist of the act of making something (a product) from raw materials and the companies that buy certain product as inputs and processes (transforms) these inputs to a value added final product for sale are categorized as manufacturing companies. The economic strength of a country is measured by the development of manufacturing industries in its regime. Manufacturing sector fuels growth, productivity and employment, and strengthens agriculture and service sectors. The sector runs with long term finance and working capital and the present study is intended to examine the relationship between the two.

Keywords: Manufacturing Sector, Growth, Productivity, Employment, Long Term Finance, Working Capital.

INTRODUCTION: FINANCE

Finance, which is a branch economics concerned with resource allocation as well as resource management, acquisition and investment, is often defined simply as the management of money or fund management. Finance is the life-blood of every business enterprise. All business decisions involve finance. Where finance is needed, the role of finance manager is inevitable. Financial management deals with rising of funds from various sources, dependent on availability and existing capital structure of the organization. The sources must be suitable and economical to the organization. Emphasis of financial management is more on its efficient utilization, rather than rising of funds, alone. The scope and complexity of financial management has been widening, with the growth of business in different diverse directions. As business competition has been increasing, with a greater pace, support of financial management is more needed, in a more innovative way, to make the business grow ahead of others. Financial Management is nothing but management of the limited financial resources the organization has, to its utmost advantage.

Resources are always limited, compared to its demands or needs. This is the case with every type of organization that is proprietorship or limited company, be it public or private, profit-oriented or even non-profitable organization. All activities, be it production, marketing, human resources development, purchases and even research and development, depend on the adequate and timely availability of finance both for commencement and their smooth continuation to completion. Every business enterprise needs two types of funds for its establishment and carrying out routine operations. Long-term funds are required to create production facilities through the purchase of fixed assets such as land and buildings, plant and machinery, furniture and fixtures and so on. Investment in these assets represents the fixed capital. Short-term funds or working capital needed for financing short-term or current assets such as cash, marketable securities, debtors and inventories. Working capital management includes maintaining the optimal balance of working capital components such as receivables, inventory and payables and using the cash efficiently for day-to-day operations. Both long-term and working capital sources are required for establishment and carrying business operations.

Working capital finance creates friction to smooth running of business. Deficient or excess working capital is not advisable, since it will lead for loss or wasting resources. Working capital management contains a proportion of working capital components that is, inventory, receivables and payables and the use of cash effectively for attaining profitability.

Proper optimization of working capital balance means minimizing the working capital requirement and realizing maximum possible revenues. The amount of profit can be a good measure of the performance of a company, so we can use profitability as a measure of the financial performance of a company as well as, and profitability is the promise for a company to remain a going concern in the world of business. Proper working capital management ensures that the company increased its profitability.

STATEMENT OF THE PROBLEM

One of the major changes involved in development is industrialization. Industrialization is the key to restructure the economy. It is the advancement of a community along with involving new and better methods of production and expanding the size of the firm. Industrialization is an effective instrument of growth and welfare. It has been defined as a process in which changes of series of strategic production functions are taking place. It involves three basic changes that accompany industrialization, mechanization of an enterprise, building of a new market and exploitation of a new territory. When we go deep into the process of industrialization the analysis of various operational aspects of the firm becomes imperative because a firm is the constituent unit of every industry and hence, plays a vital role in the industrialization, where as an industry consists of firms producing identical or close substitutes for some and relatively distant substitutes for all other outputs. Any such subgroup may be called industry. In the journey to economic growth of an economy, manufacturing sector, which itself is a corporate plays a pivotal role.

In a manufacturing concern, corporate finance basically deals with three decisions: financing decisions, investment decisions and dividend decisions. It is very important for a business organization to understand the way to manage financial resources efficiently by identifying proper mix of finance which may be a combination of spontaneous, short-term and long-term sources. Working capital management is a very important component of corporate finance since it affects the profitability and liquidity of a company. It is necessary for every business organization to manage the working capital effectively as it is essential for short-run corporate solvency or for the survival of the organization. Further, the manufacturing companies by efficiently managing the funds required for working capital could react quickly and appropriately to unanticipated changes in market variables such as, interest rates, raw material prices. This helps to gain competitive advantages over its rivals.

Manufacturing firms, which are looking for new ways to stimulate growth, improve financial performance and reduce risk in today’s challenging economic climate, often face problems with long term and working capital sources. The firms tend to utilize the long term funds acquired or kept for expansion and capital investment into the working capital cycle which affects the overall growth of the company. The corporate also tend to utilize the working capital fund which is planned for its usage in day to day operation into its long term investment or assets. This in turn affects the business growth and also the profitability of the company. Unless such funds are released from the long term sources, for the day to day operations, it becomes a very difficult task to manage the smooth operation and revenue growth of the company. Thus, the present study is undertaken to address the following research objective;

1. To examine the relationship between long-term debt and working capital in manufacturing companies.

RESEARCH METHODOLOGY

The present study is descriptive and analytical and is purely based on the secondary data. The required data have been collected from the depository of the Bombay Stock Exchange and the Centre for Monitoring Indian Economy (CMIE) Prowess and the published annual financial reports of the companies of the sample companies. The present study covers a period of 10 years from 2010 - 2011 to 2019 - 2020. Based on the purposive or judgment sampling the companies fulfilling the condition of having annual sales turnover of above Rs.500 crores and actively traded in the National Stock Exchanges are being selected for the study. Hence, a total of 25 companies that tops the list, having relevant data for the study, from NSE out of 84 companies.

Table 1: Sample Companies for the study

S. No.	Company	Business involved
1	Vedanta Limited	Mining company
2	Bharat Heavy Electricals Limited	Power generation equipment manufacturer
3	Sundram Fasteners	Powder metallurgy part manufacturing company
4	Cipla	Pharmaceutical company
5	Maruti Suzuki	Automobile manufacturer
6	Kajaria Ceramics	Ceramic wall and floor tile manufacturing company
7	Supreme Industries	Plastics pipe company
8	Coromandel International	Fertilizers, pesticides and specialty nutrients
9	Indian Oil Corporation	Petroleum refining company
10	Chambal Fertilisers & Chemicals Limited	Manufacturers of fertilisers and chemicals
11	Tata Motors	Automotive manufacturer
12	Whirlpool Corporation	Home appliance company
13	Bajaj Auto	Two-wheeler and three-wheeler manufacturing company
14	Hindalco Industries	Aluminium and copper manufacturing company
15	Polycab India Limited	Electrical products
16	Voltas	Home appliance company

17	Bharat Electronics	Aerospace and defense electronics company
18	Hindustan Aeronautics Limited	Aerospace and defense company,
19	Mahindra & Mahindra	Automotive manufacturer
20	Sun Pharmaceutical Industries Ltd.	Pharmaceutical company
21	Aarti Industries	Chemical manufacturing company
22	Madras Rubber Factory	Tyre company
23	Castrol India	Automotive and industrial lubricant manufacturing company
24	Ashok Leyland	Vehicle company
25	Biocon	Biopharmaceutical company

RELATIONSHIP BETWEEN LONG-TERM DEBT AND WORKING CAPITAL

Managing long-term funds required for fixed as well as for permanent working capital and short-term funds for temporary working capital is much important for a business organization. In the manufacturing sector, the capital for purchasing assets and for day-to-day operations is high. Here an attempt is made to identify relationship between long-term debt and working capital.

TABLE 2: RELATIONSHIP BETWEEN LONG-TERM DEBT TO WORKING CAPITAL OF SELECT MANUFACTURING COMPANIES

Year	**Long-Term Debt**	**Working Capital**	**Ratio**
2010-11	93407.31	75511.31	80.8409
2011-12	112207.02	90004.73	80.2131
2012-13	126015.12	122679.6	97.3531
2013-14	169261.89	119016.87	70.3152
2014-15	168838.36	129613.79	76.7680
2015-16	166834.03	138176.56	82.8228
2016-17	132474.91	157963.12	119.2400
2017-18	119584.35	164745.24	137.7649
2018-19	139104.05	188069.15	135.2003
2019-20	160979.79	208824.93	129.7212

Source: Annual Reports of select companies

The table above represents the relationship between long term finance and working capital of select manufacturing companies in India. The ratio shows the presence of relationship between the chosen variables and also been found increased with the year increases. It can be concluded that the working capital requirements were large dependent on long term finance of the select companies.

CONCLUSION

India's manufacturing base, which is the fourth largest among emerging economies, is among the fastest growing and has seen more investments as a proportion of gross domestic product than any country except China. After the IT boom, a manufacturing revolution has been well underway in the Indian economy, spurred on by the increasing presence of multinationals, scaling up of operations by the domestic companies and expanding domestic market. Such is a kind of significance being held by manufacturing sector of India and thus a study in any aspect of manufacturing sector is inevitably important. Its imperative to study the financial structure of manufacturing sector that consists of long term finance and working capital. The study concludes by finding a positive relationship between the two and further stating that the working capital is dependent of the long term finance of the select companies.

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