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IMPACT OF WORKING CAPITAL ON NET WORTH OF COMPANIES

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Abstract

In this research paper we found that working capital have an impact on profitability ratio of selected companies from financial year 2017-2022. For this research we calculate the working capital ratio and net worth ratio. Working Capital is independent variable and Net worth Ratio is dependent variable. Secondary data has been used for this research paper.

During the analysis, found that working capital has significant positive impact on net worth ratio. In this research, takes information Technology based companies which have highest market capitalization (BSE500 index).

Keyword: Net Worth, Working Capital, linear Regression analysis

1. Introduction of working capital

Working capital is the total of cash and highly liquid investment that a business has on hand to pay day to day operations. It indicator of the short term financial position of the organisation and it also measure the overall efficiency of the business.

Working capital also refers to liquidity level of the businesses for managing daily expenses and cover inventory, cash, account payable, account receivable and short term debt.

Working capital generally is the liquid part of the whole capital of an organization to meet the daily operations. It is basically a financial term which is used in firm for daily purpose. WC defines the liquidity condition of the organization. Shortage of funds for working capital has caused many businesses to fail. Lack of efficient and effective utilization of working capital leads to earn low rate of return on capital employed or even compels to sustain losses. The requirement of working capital varies from firm to firm depending upon the nature of business, production policy, market conditions, seasonality of operations, conditions of supply etc.

1.1.Meaning of working capital

Working capital to a firm is like the blood to human body. It is the most vital ingredient of a business. Working capital means the amount of current assets that a firm has to maintain for its day to day operations. It also involved the current assets of the business. It represents the operating liquidity available to a business, organization or other entity.

If a firm has positive working capital that means it has enough to cover short term debt. And if current liabilities exceed current assets then a company has a working capital deficiency or working capital deficit.

In other words; working capital is equal to the total of a company's current assets minus its totally current liabilities.

1.2.Working capital=current assets- current liabilities

Current assets: Include cash and assets that can be turned into cash within one year.

Current liabilities: Include debts due within one year of the date of financial statements.

The term working capital refers to the portion of total capital that is used to run a business efficiently and regularly. It is also known as short-term capital, circulating capital, or liquid capital. WC is also known as net working capital, short term capital and circulative capital.

Return on net worth indicates the profitability of the company by providing the picture of how much return it earns on its capital. It shows whether or not the company is efficient enough to grow its network every year for the future growth potential of the company.

A higher ratio indicates that the company is utilizing the money of the shareholders in an efficient manner.

On the other hand, a lower ratio indicates that the company is not using the money efficiently. It is not investing the cash in a good opportunity

2. Literature Review

Jana Debabrata(2018) Researcher found that working capital have important role in company profitability and liquidity of the company. Author examines the efficiency and relationship of the working capital management strategies of (FMCG sector Company in India). Secondary data has collected from all the 15 listed (FMCG) Company from 2013-2017. Efficient management of working capital for FMCG Company not only has a positive relationship with profitability but significantly impacts on such firm's profitability.

Hoque Ariful at all (2015) In this study researcher found that positive correlation between the profitability and working capital and negative impact on profitability ratio due to day sales outstanding . This study has used only secondary data and 3 years accounting period of six cement companies of Bangladesh to find of the relationship between the profitability ratio and working capital components.

Singhania, Monica at all (2014) researcher found the relationship between working capital management strategies of a firm and its productivity. Author found that results reveal that cash conversion cycle of a company has a negative correlation with productivity. They suggested that managers can develop the performance by declining the numeral of days receivables and rising the numeral of days payables.

Ajibolade Solabomi Omobola at all (2013) in this study author found that negative relationship between working capital and their capital structure but positive relationship between profitability and debt structure. In this study used 35 manufacturing companies listed on the Nigerian stock exchange for a two-year period (2011-2012) and Factorial-ANOVA estimation techniques has used to analyzed association between these variables.

Chatterjee Saswata (2012) The author analyzed that strong negative relationship between the components of working capital and profitability ratio and size of firm and profitability have positive relation when firm increased firm size than it lead to increased profitability of firm. In this study used secondary data, Descriptive Statistics, Pearson's Correlation, Regression Analysis and two financial years of 100 listed companies in the Bombay stock exchange to find the relationship these variables**.**

Rahman Mohammad (2011) researcher conduct the analysis on Textiles Industry has an any role in the socio-economic progress of Bangladesh. Author found the profitability is not satisfactory of this industry. In this research paper he analysis the working capital and profitability ratio analysis of this company and found the correlation and regression analysis. Researcher found that working capital has a positive impact on profitability ratios.

3. RESEARCH METHODOLOGY

Research methodologies

3.1. Objective

- To find impact of working capital on profitability ratios

3.2. Research Design in Study: In this research study empirical research design has been used.

3.3.Scope of the Study: The study focuses on the working capital of the companies and critical analysis of net worth of companies in Indian information technology sector.

3.4.Sample size for this analysis information technology sectors has been selected from BSE-500 index. Five companies have been selected based on market capital annual report companies and market capitalization. Data for these companies has been analysed from financial year 2016-17 to 2020-21. Return on net worth and working capital has been used for data analysis. The data related to the study has been collected from secondary sources such Websites

3.5.Hypothesis of study

These hypotheses are related to the study ‘‘impact of working capital on profitability ratios’’.

Following hypothesis are made

- H_{01}: There is a significant impact of working capital of company on net worth of company.
- H_{11}: There is a non-significant impact of working capital of company on net worth of company.

3.6.Research tools:

Return on net worth

Return on Net Worth (RONW) means the amount of profit or earnings a company generates on the sheer strength of its shareholders’ equity.

RoE = Net profit/ shareholders’ equity

Return on net worth ratios= The ratio shows how much profit a company generates with the invested money of equity shareholders

Working capital = (current assets -current liabilities)

Working capital ratio = (current assets /current liabilities)

Regression analysis has been conducted for find impact of working capital on profitability.

3.7.Regression equation impact of firm size, value, age and profitability on Intangible Assets disclosure

- Net worth $=\alpha + \beta 1$ working capital +E

Table 1: Model Summary (Impact of working capital ratio on return on net worth ratio).

SUMMARY OUTPUT

Regression Statistics	
Multiple R	0.914992736
R Square	0.837211707
Adjusted R Square	0.782948943
Standard Error	0.694459495
Observations	5

a. Dependent Variable: Return on Net Worth

b. Independent Variable: Working Capital

Table 1 show that, the total variation in the dependent variable explained by independent variables and has R value is 0.91, R values which range ‘between’ -1 to +1. The R value is 0.91shows that working capital has a relationship with return on net worth of companies. R square values which range lies ‘between’ 0 to 1. R square value is 0.83 which means that means83% variation in return on net worth it is explained by independent variable

Table 2: ANOVA (Impact of working capital ratio on return on net worth ratio).

.	*Df*	*SS*	*MS*	*F*	*Significance F*
Regression	1	7.440930027	7.44093003	15.4288437	0.02936982
Residual	3	1.446821973	0.48227399		
Total	4	8.887752			

a. Dependent Variable: Return on Net Worth
b. Independent Variable: Working Capital

Table 2 shows that, F value is 15.42. Its significant value is less than 0.05 it means that the return on net worth ratio has the relationship between working capital of the companies. Table 2 shows that, the regression model is fit for this analysis

Table 3: Coefficients (Impact of working capital ratio on return on net worth ratio).

	Coefficients	*Standard Error*	*t Stat*	*P-value*	*Lower 95%*	*Upper 95%*	*Lower 95.0%*	*Upper 95.0%*
Intercept	33.62286137	2.25392277	14.917486	0.000653736	26.44987318	40.79584956	26.44987	40.79584956
Working capital	-2.710042312	0.689936914	-3.92795668	0.02936982	-4.905729494	-0.51435513	-4.90573	-0.51435513

a. Dependent variable: Return on Net Worth

Table 5 shows that, impact of working capital on its return on net worth of companies. The table shows that working capital of companies. Coefficient value is 2.71 it means that firm value has positive significant impact on return on assets, its p value is 0.029. It means, it is significant because significant value lies between 0.01 to 0.05. P> 0.05