JETIR.ORG ISSN: 2349-5162 | ESTD Year : 2014 | Monthly Issue
JOURNAL OF EMERGING TECHNOLOGIES AND INNOVATIVE RESEARCH (JETIR)
An International Scholarly Open Access, Peer-reviewed, Refereed Journal

"Liquidity Analysis of Selected Cement Companies"

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ABSTRACT

The liquidity position of the company is critical to its survival. The liquidity of a firm should neither be excessive nor be very low since too much of liquidity will result in accumulation of current assets which do not yield income to the firm. The concept what constitutes the liquidity of a firm has been viewed differently by different people with reference to a business firm. Liquidity is measured by the availability of cash whether direct or indirect and involving conversion of some assets into each to meet ordinary or Extraordinary demands upon it.[1] Liquidity refers to cash and cash availability, and it is from current operations and previous accumulations that cash is available to take care of the claims of both the short-term and long-term suppliers of capital. In each of these contexts, liquidity refers to the ability of a firm to provide cash to meet the claims, the supplier of capital have on the firm.

Liquidity ratios measure the company's ability to meet its current obligations – ability to pay its obligations as and when they become due. They show whether the company can pay its short term obligations out of short term resources or not. Liquidity ratios establish a relationship between cash and other current assets to current obligations.

A company should ensure that it does not suffer from lack of liquidity or on the other hand it is not highly liquid. A low liquidity may result in the failure of meeting company's short term liabilities which may carry a bad name to the company, loss of creditor as confidence and unnecessary law suits. A very high degree of liquidity is also bad because the funds are unnecessarily tied up in current assets which earn nothing. A striking balance is necessary.

Key Words : Cement, Cement Companies, Liquidity Ratios, Liquidity Analysis etc.

INTRODUCTION: The liquidity position of the company is critical to its survival. The liquidity of a firm should neither be excessive nor be very low since too much of liquidity will result in accumulation of current assets which do not yield income to the firm. The concept what constitutes the liquidity of a firm has been viewed differently by different people with reference to a business firm. Liquidity is measured by the availability of cash whether direct or indirect and involving conversion of some assets into each to meet ordinary or Extraordinary demands upon it.[1] Liquidity refers to cash and cash availability, and it is from current operations and previous accumulations that cash is available to take care of the claims of both the short-term and long-term suppliers of capital. In each of these contexts, liquidity refers to the ability of a firm to provide cash to meet the claims, the supplier of capital have on the firm.

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SIGNIFICANCE OF THE STUDY: Cement plays a vital role in the construction of modern India, is challenging other nations in the global arena. The development of infrastructure in India is in its rapid phase and must be properly curved so that India is ahead of other countries.

In this situation, the problems related to effective financial management will help financial institutions, government agencies and other legal regulators to take the proper steps in planning the various infrastructure development projects in the Indian economy.

Although many studies have been conducted in this direction, the present would be of greater importance to many. It would help to understand the pattern and structure of the liquidity analysis of the selected companies.

REVIEW OF LITERATURE: Effective policy formulation always needs a thorough and continuous search into the nature of the reasons for, and the consequences of organisation. In line with this, some related earlier studies conducted by individuals and institutions are reviewed to have an in-depth insight into the issues of liquidity analysis. An overall view of a few studies is presented below.

Reddy and patker (2004)[1] have attempted to make a comparative study on SBI and CAN bank factors of working capital and liquidity management in factoring, based on the following objectives – to study the size composition of working capital and to evaluate the liquidity management through ratio analysis and to examine the relationship between liquidity and profitability. It is concluded that the higher liquidity is maintained in CAN Bank

correlations which is inversely related with other. It implies that as the liquidity increases the profitability decreases.

C. Narware and Vivek Sharma (2004)[2] conducted a study based on the objectives to assess the efficiency of the liquidity management of the company of HPCL and to examine the liquidity position of the company by training measure of cash and bank. It was observed from the analysis that the liquidity position of the company is very poor and the liquid assets were not sufficient in meeting the short term liabilities. In sum, the liquidity management of HPCL is very poor and is not satisfactory.

Hamasalakshmi and Manickam (2005)[3] in their study on "Financial Performance Analysis of Selected Software Companies", examined liquidity, profitability and leverage position of thirty four software companies during the period 1997-98 to 2001-02 by using ratios, correlation and multiple regression analysis. The study revealed favourable liquidity and working capital position. It is concluded that the companies rely on the internal financing and overall profitability position of the software companies showed a moderately increasing trend.

Amalendu Bhunia (2007)[4] in the study on 'Liquidity management of Sponge Iron India :A Case Study" an attempt was made to examine and evaluate the liquidity management of the public enterprise as a factor responsible for poor performance in the iron and steel industry in India covering a period from 1991-92 to 2002-03. In the course of analysis in this study, accounting tool and statistical technique have been used. Accounting technique includes ratio analysis, while statistical technique includes arithmetic mean, standard deviation and co-efficient of variation. To examine the pros and cons of the management of short-term liquidity of the company, he compared the various liquidity ratios with that of the industry average being considered as standard one. The study has identified current ratio, liquid ratio and cash position ratio is more than grand industry average during 12 years under the period of study. Hence, it can be concluded that the liquidity management of sample companies is good and satisfactory.

C.T. Sam Luther (2007)[5] has analyzed the liquidity of Madras Cements setting the objectives to measure and evaluate the liquidity position of the company, to assess the correlation between liquidity and profitability, to assess the trade-off between profitability and risk. The relationship between liquidity and profitability has been measured by using Spearman's Rank Correlation Coefficient. This is also further tested by using the Students' t-test. An attempt is also made to analyses the trade-off between the risk and profitability, the risk analysis of working capital management has been done to assess the extent of current assets maintained by the company, adequate enough to meet the current obligations and also to support the given level of operation. Enterprises are said to follow an aggressive approach when the current assets are financed only by short-term sources and a conservative approach when the current assets are financed by both short term and long term sources. The author has made a finding that the company has adopted aggressive policy has made a negative impact on its profitability.

The company has adopted a conservative policy of working capital for the first half of the study period and thereafter in a more aggressive mood. It is concluded that it is the right time for the company to control the working capital so as to meet any sort of financial distress that may occur in future.

Adolphusj. Toby (2008)[6] in his study on "Liquidity Performance Relationship in Neigerian Manufacturing Companies (1990-2002)" has analysed the empirical relationship between liquidity and other performance measures in Nigerian manufacturing companies between 1990-2002. Using date from 87 quoted manufacturing companies, ten multiple regression models were estimated with four liquidity measures as independent variables, and ten others covering profitability, efficiency and leverage measures as dependent variables. The results show statistically significant relationship between liquidity and profitability, efficiency and leverage measures

RESEARCH GAP : After thorough analysis of existing literature, it is found that, though several studies on the subject of liquidity analysis have been conducted the explorations on the subject have been meager. Particularly on cement industry which is growing at a rapid speed and is gaining importance. In view of the above studies and the importance of liquidity analysis, the present study is to analyse the liquidity position of selected cement companies.

OBJECTIVES OF THE STUDY : The following are the objectives of the study:

1. To study about the financial position of selected cement companies.
2. To analyse the liquidity position of selected cement companies and
3. To offer suitable suggestions for the growth of cement companies.

LIMITATIONS OF THE STUDY : In a study of this magnitude though, meticulous care has been taken in each and every aspect of study. Certain limitations are likely to be there in the study.

- A study is confined to 10 years data from 2008-2018.
- The study is completely based on secondary data.

DATA ANALYSIS

Table No. 1. Liquidity Analysis of Sample Companies

Cement Company	Mean	S.D.	C.V. (in Percentage)
Madras Cements	2.043	0.259	12.68
India Cements	3.703	1.311	35.40
Chettinad Cements	2.011	0.354	17.60
Dalmia Cements	3.025	0.278	9.19
Andhra Pradesh Cements	2.074	0.412	19.86

Source: Computed Data.

It is observed from Table No. 1 that on the average of 10 years, India Cements is placed in a good liquidity position (3.703) with a low liquidity of Chettinad Cements (2.011). The C.V. is high with India Cements (35.40%) and is low with Dalmia Cements with 9.19 per cent.

It can be further observed that a company is said to be financially sound if it is in a position to carry on the activities in a smooth manner, meeting its vendor obligations, either long, medium-term or short term, without any difficulty. It indicates the availability of current assets in rupees for every one rupee of current liabilities. It is a well laid principle in finance that short term funds should take care of short term requirements and long term inflow to match the long term requirements. These ratios, are hence called 'short term solvency ratios'.

Liquidity is an important index of the financial strength of any company or organisation. The liquidity values of different companies are taken for observation and studied for a period of 10 years. It is proposed to investigate whether the liquidity values of the companies put together on the average is the same for different years.

It is also proposed to test the validity of null hypotheses.

H01: The average of the liquidity value of the selected cement companies do not differ significantly over the years.

H02: The average liquidity values do not differ significantly between the companies for the period of 10 years.

Using ANOVA two way classification procedures, the following results are obtained and it is presented in Table No. 2.

Table No. 2. ANOVA for Liquidity Analysis

Source of Variation	SS	Df	MS	F	P-value	F-cirt
Rows	4.6177	9	0.512974	1.247777	0.298205	2.152607
Columns	23.2467	4	5.811675	14.13653	0.0049	2.633534
Errors	1.79998	36	0.411111			
Total	42.66345	49				

From Table 5.2, the following conclusions are drawn

The F value corresponding to the years (rows) is F = 1.2477 with a corresponding p = 0.2982. Hence, H01 is accepted. This implies that there is no significant difference between the averages of the liquidity of the companies over 10 years.

ii. The F value corresponding to the companies (columns) is F = 14.1365 with p = 0.0049 which is significant. Hence, H02 is rejected. This implies that on the average, liquidity values of the different cement companies differ significantly.

Inventory Turnover Ratio : This ratio indicates the number of times inventory is replaced during the year. It measures the relationship between sales and closing inventory level. In general, a high inventory turnover ratio is better than the low ratio. A high ratio implies good inventory management where the old inventories are pushed out in the market and what is remaining in stock is fresh. So, even for items of less shelf storage, high inventory turnover ratio is preferred. Yet a very high ratio calls for a careful analysis. Thus, a company should have neither too high nor too low inventory turnover. To avoid both 'stock out costs' associated with a high ratio and the costs of carrying excessive inventory with a low ratio, what is suggested is a reasonable level of this ratio. The mean values and C.V. of inventory turnover ratio over the successive years for the sampled companies are given in Table No. 3.

Table No. 3. Inventory Turnover Analysis of Sample Companies

Cement Company	*Mean*	*S.D.*	*C.V.* *(In Percentage)*
Madras Cements	23.62	6.83	28.94
India Cements	13.18	2.50	18.99
Chettinad Cements	19.02	8.48	44.59
Dalmia Cements	4.98	1.37	27.43
Andhra Pradesh Cements	13.23	3.53	26.66

Source: Computed Data.

It is evident from Table No. 3 that on considering the average of 10 years, Andhra Pradesh Cements is placed in a good inventory turnover position (23.62) with a low inventory turnover of Dalmia Cements (4.98). The C.V. is high (44.59%) with Chettinad Cements and is low (18.99%) with India Cements.

Appears that Dalmia Cements is preferred to Madras Cements based on the Inventory Turnover Ratio. Inventory is an important index of the financial strength of any company or organization. The inventory turnover values of different companies are taken for observation and studied for a period of 10 years. It is proposed to investigate whether the inventory turnover values of the companies put together on the average is the same for different years. It is also proposed to test the validity of null hypotheses.

H01: The average of the inventory turnover value of the selected cement companies do not differ significantly over the years.

H02: The average inventory turnover values for the period of 10 years do not differ significantly between the companies.

Using ANOVA two way classification procedure, the following results are obtained and it is presented in Table No. 4.

Table No. 4. ANOVA for Inventory Turnover Ratio

Source of Variation	*SS*	*Df*	*MS*	*F*	*P-value*	*F-cirt*
Rows	547.8065	9	60.86739	2.594498	0.020308	2.152607
Columns	1971.274	4	492.8184	21.00659	5.25E-09	2.633532
Errors	844.5666	36	23.46018			
Total	3363.647	49				

From Table No. 4, the following conclusions are drawn

The F value corresponding to the years (rows) is F = 2.5945 with a corresponding p = 0.0203. Hence, H01 is rejected. This implies that there is significant difference between the averages of the inventory turnover of the companies over 10 years.

The F value corresponding to the companies (columns) is F = 21.0066 with p = 0.0000 which is significant. Hence, H02 is rejected. It is concluded that on the average, inventory turnover values of the different cement companies differ significantly.

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