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A Comparative Study on Working Capital Management and Cash Flow Analysis Practices of Selected Companies in FMCG Industry

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ABSTRACT

The paper examines the working capital management practices and cash flow statement of well-known firms in Fast- Moving Consumer Goods (FMCG) industry in India. The present study is focused on Hindustan Unilever Limited (HUL) and Godrej Consumer Products Limited (GCPL) as these companies are reputed in FMCG sector.The study is an attempt to analyze and evaluate working capital management practices through various parameters like; current ratio, quick ratio, inventory turnover ratio debtor's turnover ratio and fixed asset turnover ratio etc. The Cash flow analysis is conducted with the help of indirect cash flow method. The necessary data has been collected for the period of six years from financial year 2012-13 to financial year 2017-18 for working capital management whereas data has been collected for the period of five years from financial year 2013-14 to financial year 2017-18 for cash flow statement.

Keywords: Working capital, ratios, FMCG sector, cash flow statement.

INTRODUCTION:

Fast Moving Consumer Goods are generally low cost commodities that are sold very quickly and at comparatively low cost. It includes non-durable goods such as packaged goods, beverages, toiletries and other consumables. It is considered a unique business model that requires competitive advantages in areas such as manufacturing, branding and advertising.

Working capital management:

Working capital management is one of the most significant functions of corporate management. Every organization whether public and private, profit oriented or not, irrespective of its size and native of business, needs adequate amount of working capital. Working capital is one of the powerful measurements of the financial position.
Working capital is the capital of a business which is used in its day-to-day trading operations, calculated as0.the current assets – current liabilities and measure company's efficiency and its short-term financial health. The popular formula to find out working capital is as under.

Working capital = current assets-current liabilities:

The aim of working capital management is to manage the firm's current assets and current liabilities in a way that a satisfactory level of working capital is maintained. The efficient management of working capital minimizes the cost and does much for the success of the business.

Cash Flow Statement:

Cash flow statement is a very important financial statement, as it reveals how much cash the company is actually generating. A statement of cash flows should be presented as an integral part of financial statements. Every company's financial performance is not so much dependent on the profits earned during a period, but more realistically on liquidity or cash flows. Cash flow statement includes three activities; Operational activities, Investing activities, Financing activities. Activities that are directly related to the daily core business operations are called operational activities. i.e. sales, marketing, manufacturing, technology upgrade, resource hiring etc.Activities pertaining to investments that the company makes with an intention of reaping benefits at a later stage. i.e. investing in equity shares, investing in land, property, plant and intangibles and other non-current assets. Financing activitiespertaining to all financial transactions of the company such as distributing dividends, paying interest to service debt, issuing corporate bonds.

LITERATURE REVIEW:

It deals with all the aspects of working capital of which in depth study has been carried out as discussed below.
Natarajan Sundar (1980) believes that working capital is an important term at a national and a corporate level. According to him if we want to control the working capital at national level, first we have to control the credits. He concludes that as much as the potential corporate level investment is in the working capital, there is also important in fixed assets investment.
Bhattacharyya Hrishikes (1987) has tried to develop the tools and comprehensive theory of working capital management from the system point of view. For this, finance manager always try to balance both the things assets and capital of the balance sheet. His main objective is to see how the net worth of business is increased without increasing the riskness of the business.
Rao K. V. and Rao Chinta (1991) have tried to analyze the strong and weak point of conventional techniques of working capital. The result has been obviously mixed while some of conventional theory gave good results and others failed to do his job. The authors have tried to evaluate the working capacity of the working capital management from the help of conventional techniques e.g. ratio analysis. The article concludes that working capital decision is a comprehensive and yardstick in evaluation of the working capital efficiency.
Hossain SaiyedZabid and Akon Md. Habibur Rahman (1997) are focused on the basic objective of the working capital management i.e. to arrange the required working capital funds at the right cost, right time and from right origin with a view to attaining differences between liquidity and profitability.
Singaravel, P. (1999) emphasis on the interdependence among working capital, liquidity and profitability; of which adequate liquidity have given them the most first preference followed by adequate working capital and profitability. The article is explained about the liquidity analysis in- depth and stated its interrelationship with working capital and profitability. As the working capital, liquidity and profitability three are described in a triangular position, none is dependable at the satisfaction of the other. Alternatively, the working capital requirements are considered for long – term funds which affect the profitability.
Garg Pawan Kumar (1999) throws light on the study of working capital trend and liquidity analysis of the Haryana's selected public sector enterprises. The study is most likely to suggest the components of the working capital requirements. After seeing the facts author realized that the proper assessment need and predicting of working capital in the public sector undertaking.
Kaur Harsh V. and Singh Sukhdev (2013) this article emphasis on the ratio of output to the input of cash conversion and setting up the days of operating cycle. The study examines the relationship between the profitability and working capital achievement calculated by income to total assets and income to current assets. Authors studied with listed companies in BSE 200 that is consider more than 19 industries for the period 2000 to 2010.
Kovelskiy (2015) analyzed the different sources of financing the working capital of a firm and the main objective for effective utilization of the working capital requirements. The study employed survey method for data collection and focuses much on how smoothly gets completed the day- to- day operation of the firm; working capital management plays a significant role.

METHODOLOGY:

The main objective of this study is to examine the working capital management and cash flow statement analysis practices in the FMCG sector. For this, two companies are selected Hindustan Unilever Limited and Godrej Consumer Products Limited. The market capitalization of HUL as on 17th March was stood at Rs. 339668.68Crore where as the market capitalization of GCPL as on 17th March was stood at Rs. 65,710 Crore.The important variables considered for working capital are current ratio, quick ratio, inventory turnover ratio, debtor's turnover ratio and asset turnover ratio. The required data has been collected from the database capitalize and annual reports of the companies for a period of six years. On the basis of data collection here working capital and cash flow statement are analyzed.

INDUSTRY AND COMPANY PROFILE:

The large players in Fast –Moving Consumer Goods (FMCG) industry includes Hindustan Unilever Limited, Nestle India, Godrej Consumer Products Limited, Indian Tobacco Company, Procter and Gamble, Dabur India Limited, Nirma, Emami, Haldiram's, Patanjali Ayurved, Coca- Cola India, Pepsi-Co etc. This study focuses on two companies i.e. Hindustan Unilever Limited and Godrej Consumer Products Limited in FMCG sector. The profile of the selected companies is as follows:

Hindustan Unilever Limited (HUL) is the India's largest fast – moving consumers goods company. It was established as Lever Brothers in India in 1933 followed by its merger with Hindustan Vanaspati Manufacturing Co.Ltd.And United Traders Ltd.rechristening by the name of Hindustan Lever Limited in 1956. The company received its final (current) name in June 2007 as Hindustan Unilever Limited. HUL provides home – care, personal care, foods and refreshments includes a portfolio of brands that serves consumers across the length and breadth of India. During the period it has acquired several companies like, its acquisition with Brook Bond (1984), Lipton Tea (1972) and also merged with Tata Oil Mills Company (TOMCO), merged with HLL (1993), Lakme India Limited (1995).

Godrej Consumer Products Limited (GCPL) is an Indian consumer goods company based in Mumbai, India. GCPL's products include soap, hair colourants, toiletries and liquids detergents. It also includes 'Cinthol', 'Godrej Fair Glow', 'Godrej No.1', and 'Godrej Powder Hair Dye'. Founded in 2001; during the year 2002-03 the company launched Godrej No.1 Ayurvedic soap and Godrej Fair Glow Saffron in the Southern markets of Karnataka and Andhra Pradesh.

FINDINGS AND DICUSSION:

Working Capital Analysis:

Current Ratio:

Current Ratio is a liquidity ratio that measures a company's ability to pay short –term and long –term obligations. It is calculated by dividing current assets by current liabilities. A manufacturer normally needs a current ratio of around 2:1, it means that current assets twice as large as current liabilities.

A higher current ratio indicates strong solvency position and is therefore considered better. The formula of current ratio are as follow as;

Current ratio = current assets / current liabilities

Table 1: Current Ratio of Hindustan Unilever Limited and Godrej Consumer Products Limited for the period of 2013 to 2018

Year	Hindustan Unilever Limited	Godrej Consumer Products Limited
2013	0.84	1.09
2014	0.78	0.81
2015	0.78	0.72
2016	0.92	0.80
2017	0.96	0.72
2018	0.92	0.66
Average	0.86	0.80

Source: Capitaline Database

The standard current ratio is 2:1. The current ratios for six years from 2013 to 2018 are shown in the table – 1. When we compare the ratios for both the companies; both the company's current ratio position is not up to the standard over the study period. The average current ratio is 0.86 in Hindustan Unilever Limited and 0.80 in Godrej Consumer Products Limited. So it can be said that both the FMCG companies are not good performing for current ratio because their figure also showing their situation.

Quick Ratio/ Acid Test Ratio/Liquid Ratio:
It is used to test the ability of a business to pay its short-term debts. It measures the relationship between the liquid assets and current liabilities. The formula of quick ratio/ acid test ratio/liquid ratio are as follow as;
Quick ratio = current assets – inventories / current liabilities

Table 2: Quick Ratio of Hindustan Unilever Limited and Godrej Consumer Products Limited for the period of 2013 to 2018

Year	Hindustan Unilever Limited	Godrej Consumer Products Limited
2013	0.45	0.78
2014	0.44	0.39
2015	0.47	0.58
2016	0.67	0.55
2017	0.51	0.38
2018	0.68	0.39
Average	0.53	0.51

Source: Capitaline Database

The standard quick ratio is 1:1. A company with a quick ratio of less than 1 cannot currently fully pay back its current liabilities. This ratio is considered to be much better and reliable as a tool for assessment of liquidity position of the companies.Analysis of this ratio, it is the same position of current ratio. During this study period the quick ratio of both companies not the standard quick ratio. Only GCPL company has the near to standard quick ratio in the year 2013. Both of these ratios represent the idea that the HUL has the so far an almost constant which is good at some point, but GCPL too long for this reason is not good liquidity position. So their profit margin may not so high.

Inventory Turnover Ratio:
Inventory Turnover Ratio is calculated by dividing the cost of goods sold for a period by the average inventory for that period. Higher turnover ratio is more profitable for the business.
Inventory turnover ratio = cost of goods sold/ average inventory. Where, average inventory = total inventory /2

Table 3: Inventory Turnover Ratio of Hindustan Unilever Limited and Godrej Consumer Products Limited for the period of 2013 to 2018

Year	Hindustan Unilever Limited	Godrej Consumer Products Limited
2013	10.82	7.82
2014	11.21	8.35
2015	12.23	9.57
2016	13.06	9.34
2017	14.11	9.11
2018	14.92	9.41
Average	12.72	8.93

Source: Capitaline Database

In this analysis we identify that the continuous improvement of inventory turnover ratio through the years from 2013 to 2018 in both the companies Hindustan Unilever Limited and GodrejConsumer Products Limited. Here we understand that the turnover ratio is increasing because the increasing rate of sales is higher than average inventory. Generally it is important that they are holding much more inventory, which has make up the cash balance.So, we can say that both the companies gaining much more control over inventory. However, it is higher in HUL.

Debtors Turnover Ratio:
The Debtors Turnover Ratio also called as Receivable Turnover Ratio shows how quickly the credit sales are converted into the cash. This ratio measures the efficiency of a firm in managing and collecting the credit issued to the customers. The formula of debtors turnover ratio are as follow as;

Debtors turnover ratio = annual net credit sales / average accounts receivables
Where, accounts receivables = trade debtors + bills receivables

Table 4: Debtors Turnover Ratio of Hindustan Unilever Limited and Godrej Consumer Products Limited for the period of 2013 to 2018

Year	Hindustan Unilever Limited	Godrej Consumer Products Limited
2013	36.08	35.02
2014	35.83	32.90
2015	40.92	33.33
2016	36.27	23.26
2017	34.63	20.93
2018	33.95	23.39
Average	36.28	28.13

Source: Capitaline Database

From the above table we can say that the average collection period of both the FMCG companies is decreasing. Hindustan Unilever Limited is collecting their debts for on an average 36.28 times in a year and Godrej Consumer Products Limited is collecting their debts 28.13 times in a year. A low ratio stand up the company bad collection period and it's also indicating of low cash balance. The main objective of any company should increase sale instead of increasing receivables because it makes up the cash balance. So, both the companies must be increase the average collection period.

Fixed Asset Turnover Ratio:

The fixed Asset Turnover Ratio is an efficiency ratio that measures a company's ability to generate sales from its assets by comparing net sales with average total assets. The formula of debtors turnover ratio are as follow as;
Fixed asset turnover ratio = sales / net fixed assets

Table 5: Fixed Asset Turnover Ratio of Hindustan Unilever Limited and Godrej Consumer Products Limited for the period of 2013 to 2018

Year	Hindustan Unilever Limited	Godrej Consumer Products Limited
2013	6.87	2.52
2014	6.89	2.78
2015	7.14	2.96
2016	8.44	3.32
2017	8.70	3.76
2018	7.06	3.74
Average	7.51	3.18

Source: Capitaline Database

From the above table we can say that the fixed assets turnover ratio of Hindustan Unilever Limited is better than Godrej Consumer Products Limited. Because HUL company is having more times fixed assets turnover ratio in comparison to GCPL Company.

Cash Flow Analysis:

The cash flow statement provides information about a company's cash inflows and can cash out flows over a specified period of time. Simply put, it discloses how a company spends its money (cash outflows) and where that money comes from (cash inflows).

Table 6: Cash Flow Analysis of Hindustan Unilever Limited and Godrej Consumer Products Limited for the period of 2014 to 2018

Particulars / Year	Hindustan Unilever Ltd (HUL) (In Rs. Cr………)					Godrej Consumer Products Ltd (GCPL) (In Rs. Cr………)				
	2014	2015	2016	2017	2018	2014	2015	2016	2017	2018
Cash and cash equivalents at beginning of the year	326.41	620.61	720.00	635.00	572.00	241.60	150.06	169.86	40.57	88.00
Net cash from operating activities	3724.15	3271.90	3974.00	4953.00	5916.00	749.54	782.66	512.10	1177.18	1235.44
Net cash used in investing activities	-513.16	279.90	-51.00	-752.00	-1264.00	-552.61	-453.83	-99.81	-1008.57	-302.42
Net cash used in financing activities	-2916.79	-3450.44	-4008.00	-4264.00	-4651.00	-287.93	-309. 36	-541.58	-121.18	-934.91
Net (increase/ decrease) in cash and cash equivalent	294.20	101.36	-85.00	-63.00	1.00	-91.00	19.47	-129.29	47.43	-1.89
Cash and cash equivalents at end of the year	620.61	721.97	635.00	572.00	573.00	150.60	169.53	40.57	88.00	86.11

Source: Capitaline Database

Cash flow statement includes three activities; operating activities, investing activities and financing activities. From the above table we can say that the net cash receiving from all the activities of Hindustan Unilever Ltd (HUL) is higher than Godrej Consumer Products Ltd (GCPL) and in last the cash inflows of Hindustan Unilever Ltd have more and less outflows in compare to Godrej Consumer Products Ltd.

CONCLUSION:

In this study, both the companies are trying to manage their working capital management and cash flow requirements. On comparative terms, Hindustan Unilever Ltd (HUL) is considered superior as compare to Godrej Consumer Products Ltd (GCPL). Because HUL has the higher ratios, turnover, higher collection of debts and cash/ liquidity requirements.

This article is based on two research questions. First, we analysis of liquidity measures indicates that current ratio is bad condition for both the companies and quick ratio is also found that the same position of current ratio. Second, we analysis is all efficiency measures indicates inventory turnover ratio, debtors turnover ratio and fixed turnover ratio. And we can say that Hindustan Unilever Ltd (HUL) has the higher inventory turnover, collecting more times their debts and having more times assets turnover ratio in comparison to Godrej Consumer Products Ltd (GCPL). But the cash flow of GCPL Company is not up to the level and the liquidity position of the GCPL Company has not sound in compare to HUL. Because Hindustan Unilever Ltd (HUL) company is receiving higher cash flows from all activities than Godrej Consumer Products Ltd (GCPL) company.

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