IJITECH International Journal of Innovative Technologies
WWW.IJITECH.ORG
ISSN 2321-8665
Volume.10, Issue.02,
July-December,2022,
Pages:69-73

Impact on Working Capital Profitability: IT Industry

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Abstract: The present study has been emphasized on the working capital financial ratios impact on the operating profitability of the selected IT industries. The study has considered the secondary data from the period of 2016-17 to 2020-21 year. In the study key working capital ratios were considered and measured the relationship with the bivariate correlation. The study result indicates that the all the key working capital ratios are having the significant relation with the selected operating profitability of the IT companies. The study has adopted the ordinary least square method and the result indicated that the ratios of working capital influencing the operating profitability. This study is useful to the IT industries, academicians and financial consultants.

Keywords: Working Capital Management, Profitability.

I. INTRODUCTION

The term 'working capital management' primarily refers to the efforts of the management towards effective management of current assets and current liabilities. Working capital is nothing but the difference between the current assets and current liabilities. In other words, an efficient working capital management means ensuring sufficient liquidity in the business to be able to satisfy short-term expenses and debts. In a broader view, 'working capital management' includes working capital financing apart from managing the current assets and liabilities. That adds the responsibility for arranging the working capital at the lowest possible cost and Utilizing The Capital Cost-Effectively. The primary objectives of working capital management include the following:

Smooth Operating Cycle: The key objective of working capital management is to ensure a smooth operating cycle. It means the cycle should never stop for the lack of liquidity whether it is for buying raw material, salaries, tax payments etc.

Lowest Working Capital: For achieving the smooth operating cycle, it is also important to keep the requirement of working capital at the lowest. This may be achieved by favorable credit terms with accounts payable and receivables both, faster production cycle, effective inventory management etc.

Minimize Rate of Interest or Cost of Capital: It is important to understand that the interest cost of capital is one of the major costs in any firm. The management of the firm should negotiate well with the financial institutions, select the right mode of finance, maintain optimal capital structure etc.

Optimal Return on Current Asset Investment: In many businesses, you have a liquidity crunch at one point of time and excess liquidity at another. This happens mostly with seasonal industries. At the time of excess liquidity, the management should have good short-term investment avenues to take benefit of the idle funds.

II. IMPORTANCE OF EFFECTIVE WORKING CAPITAL MANAGEMENT

Although the importance of working capital is unquestionable in any type of business. Working capital management is a day to day activity, unlike capital budgeting decisions. Most importantly, inefficiencies at any levels of management have an impact on the working capital and its management. Following are the main points that signify why it is important to take the management of working capital seriously.

- Ensures Higher Return on Capital
- Improvement in Credit Profile & Solvency
- Increased Profitability
- Better Liquidity
- Business Value Appreciation
- Most Suitable Financing Terms
- Interruption Free Production
- Readiness for Shocks and Peak Demand
- Advantage over Competitors

III. INFORMATION TECHNOLOGY IN INDIA

The IT & BPM sector has become one of the most significant growth catalysts for the Indian economy, contributing significantly to the country's GDP and public welfare. The IT industry accounted for 8% of India's GDP in 2020, and it is expected to contribute 10% to India's GDP by 2025. India's rankings improved four places to the 46th position at the 2021 edition of the Global Innovation Index (GII). India is the leading sourcing destination across the world, accounting for approximately 55% market share of the US$ 200-250 billion global services sourcing business in 2019-20. According to National Association of Software and Service Companies (Nasscom), the Indian IT industry's revenue touched US$ 227 billion in FY22, a 15.5% YoY growth.

According to Gartner estimates, IT spending in India is expected to increase to US$ 101.8 billion in 2022 from an estimated US$ 81.89 billion in 2021. Indian software product industry is expected to reach US$ 100 billion by 2025. Indian companies are focusing to invest internationally to expand their global footprint and enhance their global delivery centres. The data annotation market in India stood at US$ 250 million in FY20, of which the US market contributed 60% to the overall value. The market is expected to reach US$ 7 billion by 2030 due to accelerated domestic demand for AI. Exports from the Indian IT industry stood at US$ 149 billion in FY21. Export of IT services has been the major contributor, accounting for more than 51% of total IT export (including hardware). BPM and Engineering and R&D (ER&D) and software products export accounted for 20.78% each to total IT exports during FY21. ER&D market is expected to grow to US$ 42 billion by 2022. The IT industry added 4.45 lakh new employees in FY22, bringing the total employment in the sector to 50 lakh employees.

IV. REVIEW OF LITERATURE

Sumathi A and Narasimhaiah - A Study on the Effect of Working Capital on the Profitability of Infosys. This study has been conducted to know effect of the size and rising of working capital and whether such an investment has grown or reduced over a period of time. Objective of this study is to analyze the relationship between management of working capital and profits of the firm.

Ahmed SU, Mahtab N, Nazmul Islam and Abdullah M - Study on Impact of working capital management on profitability: A Study on Textile Companies of Bangladesh. The objective of the study is to examine the impact of different components of working capital management on profitability of the Bangladeshi textile companies. To examine that authors used 8 years data from the time period of 2007- 2014 of 22 textile companies listed in Dhaka Stock Exchange and logistic regression has used to analyze the data. The findings of the study showed that, there is statistically significant relationship between working capital management and profitability of the Bangladeshi textile companies.

Kruti A. Patel (2015) studied on the impact of working capital management on profitability of Indian Oil Corporation. The examiner turned into based totally on secondary data and study period was 2009-10 to 2013-14. Pearson correlation, descriptive statistic and INM SPSS were applied as research methodology. The results show that there is significant negative correlation among working capital management and net income and it also indicates that there's negative relationship between liquidity and profitability.

PoonamGautam Sharma and PreetKaur (2015) study the impact of working capital management on profitability of BhartiAirtel Telecom employer. The study period was 2007-08 to 2014-15 and statistical and econometric equipment has been used for study. The outcomes reveals that there is significant negative relationship among liquidity and profitability of the corporation and it additionally well-known shows that quick ratio, stock turnover ratio, debtors turnover ratio of corporation indicates satisfactory performance and current ratio of company was found not satisfactory.

Dr. AregaSeyoum's, TadeleTesfay's and Tadesse's studies paper (2016) was to examine and analyze the impact of working capital management on the profitability of foods complex manufacturing companies operating around Addis Ababa from 2009 to 2013. The results provided evidence that the Cash Conversion Cycle, as a measure of working capital management, negatively impacts Return on Assets. A negative relationship between the Receivables Collection Period, strong negative relation of Inventory Conversion Period, Payment Deferral period and profitability.

JyotiMahato and Uday Kumar Jagannatham (2016) studied the impact of working capital management on profitability for the Indian Telecom Sector. Return on Assets, Average Collection period, Inventory Conversion period, Average collection period, Cash Conversion Cycle, Debt ratio, Current ratio, and firm size were taken as variables. Statistical tools such as, Regression analysis, multiple regression analysis, Correlation analysis, T test, F test and analysis of variance (ANOVA) and Descriptive analysis are used. The result of study shows that there is significant relationship between profitability and working capital management. The correlation analysis shows that ROA has negative relationship with ACP, ICP, CCC and Current Ratio.

Owele and Makokeyo (2015) argued that the organization's profitability rests at the operating capital management approach accompanied through manner of this kind of business enterprise. In their study on operating capital management processes and economic overall performance of agricultural corporations indexed in Nairobi Securities Exchange, the authors referred to the maximum worthwhile companies used conservative working capital management strategies at the same time as folks who used competitive capital management strategies had been much less profitable. It was further noted that companies may register high profits with reference to large assets base but although generate low profitability. This is associated with large proportions of assets being idle and consequently affecting profitability.

Zill-e-Huma, FaizaMaqbool Shah - The primary aim of the study is to assess the Impact of Working Capital on the Profitability - A Case of Pakistan State Oil. For such assessment, Pearson correlation and simple linear regression methods are applied in which the data of 10 years (2005-2014) has been taken to analyze the relationship between working capital and profitability of PSO. The result unveiled the negative relationship of debt ratio and positive relationship of current ratio with the profitability.

BojanaVukovic, Mirko Andric, DejanJaksic - This paper analyzed the Impact of the policy of Working Capital management on Profitability in the food industry in the Republic of Serbia in 2014. The sample includes 95 active companies. By applying multiple regression analysis, the influence of certain variables (CR, CATAR, CLTAR, and DTAR) of working capital management was measured on profitability (ROA). The results of regression analysis showed that most of the analyzed variables significantly affect profitability.

SidrahRizwan, FaizaMaqbool Shah - The aim of this study is to examine the impact of working capital management on firm's performance for textile spinning companies in Pakistan listed in KSE. A panel data has been used in this study for 10 sample companies that cover the period of 7 years from 2008 to 2014.Analysis for identifying the relationship between working capital management and firm's performance. The study finds a very weak negative relationship ARTO, APTO and INV.TO with ROE and ROA but statistically no relationship exists between WCM and Profitability.

Salman Sarwat - Impact of working capital management on the profitability of firms: case of Pakistan's cement sector. The aim of this study is also to find out the component wise connection between the effective management of working capital and profitability in the context of Pakistan's cement sector. Panel data of 18 companies listed in KSE from cement sector from 2007 to 2011 is collected. Efficient of working capital management is calculated through six accounting ratios. Panel least square method of regression is applied for analysis. Results suggest that assets turnover ratio (ATO), current ratio, and size of the firm have positive and significant affiliation with the Return on Assets.

Padachi (2006) studied the trend of working capital and its effect on overall performance in Mauritian firms by way of studying 58 small production corporations for 1998-2003. He used return on overall asset (ROTA) as profitability measure and concluded the negative affiliation of profitability with inventories days and debts receivables.

V. RESEARCH METHODOLOGY

A. Need For The Study

As working capital is a very important component of corporate finance because it directly affects the liquidity profitability and solvency of a business entity, which includes current assets and current liabilities. The research has thoroughly examined impact of variables involved through ratio analysis and tools like correlation and regression.

B. Scope of the Study

The study focused on assessing the impact of working capital management on the profitability of IT companies. The study investigated the extent to which the IT firms manage their working capital for 5 years, that is, 2016-2020. Mainly the study focused on working capital ratios relating with ROTA. To achieve these objectives the study used secondary data, which is extracted from the statement of financial position of IT companies such as INFOSYS, WIPRO, and TCS. The study examines the working capital and profitability of selected IT Company's. The study also gives suggestions to improve the financial performance of selected IT companies.

Objectives of the Study:

- To evaluate working capital performance of company.
- To study the impact of select ratios on corporate profitability.
- To determine the relationship between working capital management and ROTA.

VI. METHODOLOGY

The study primarily used secondary data. In this research we will see the different working capital management practices and its impact on profitability of three IT companies like INFOSYS, WIPRO and TCS for a period of 5 years from 2016-2020.

A. Sources of Data

Data collection is important for any research. There are two types of data, namely primary data and secondary data. This study is based on secondary data for all numerical data for this study were collected from the published annual reports of the companies of the sample, it will become the only source needed for this research. Data is also extracted from different websites, standard text books, Journals, etc. In this study, we have utilized the secondary data to estimate the above data. The sample size for this research is 3 companies that are listed as top companies by the market capitalization.

B. Statistical Tools And Techniques

- Liquidity Ratios
- Profitability Ratios

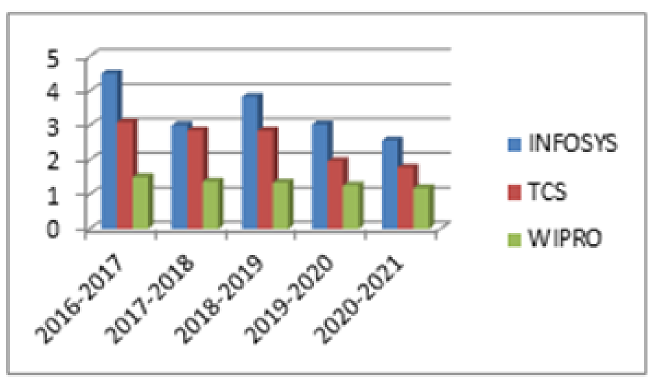
C. Period of Study

The period of study has been conducted from September 2020 to October 2020 by taking the financial ratios and various other financial statements of IT companies.

D. Data Analysis & Interpretation Liquidity Ratios

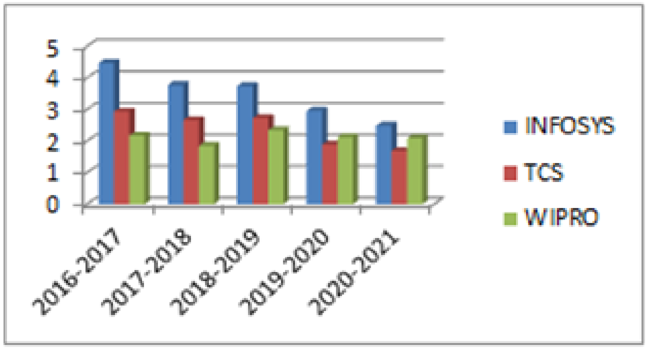
1.Current Ratio

Company/Year	2016 - 2017	2017 - 2018	2018 - 2019	2019 - 2020	2020 - 2021
Infosys	4.5	3	3.83	3.03	2.56
TCS	3.09	2.85	2.84	1.97	1.78
Wipro	1.5	1.37	1.34	1.26	1.18



2. Quick Ratio

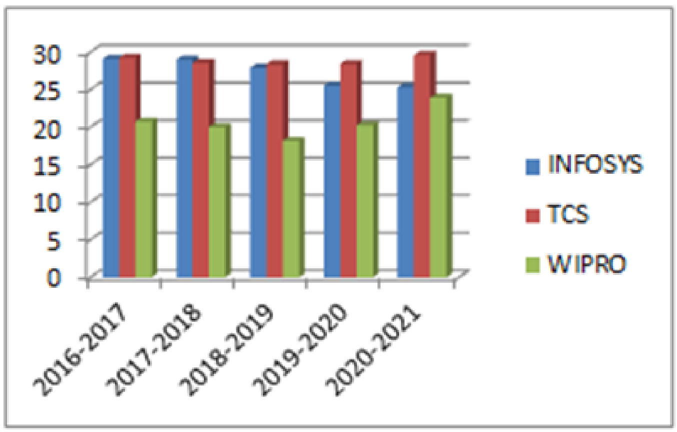
COMPANY/YEAR	2016-2017	2017-2018	2018-2019	2019-2020	2020-2021
INFOSYS	4.47	3.77	3.74	2.96	2.49
TCS	2.93	2.67	2.74	1.89	1.69
WIPRO	2.17	1.85	2.35	2.13	2.09



E. Profitability Ratios

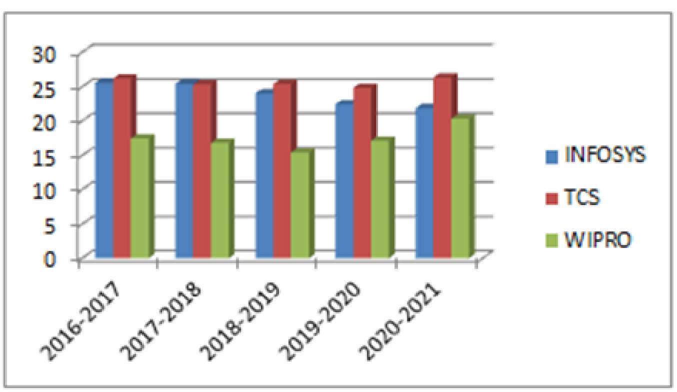
1.Operating Profit Margin Ratio

COMPANY/YEAR	2016-2017	2017-2018	2018-2019	2019-2020	2020-2021
INFOSYS	29.09	29.02	27.92	25.54	25.34
TCS	29.22	28.56	28.38	28.44	29.64
WIPRO	20.75	20.02	18.2	20.24	23.94



2. Profit before Interest and Tax Margin Ratio

COMPANY/YEAR	2016-2017	2017-2018	2018-2019	2019-2020	2020-2021
INFOSYS	25.6	25.46	24.08	22.5	21.88
TCS	26.23	25.35	25.41	24.9	26.35
WIPRO	17.47	16.82	15.43	17.1	20.31



VII. CONCLUSION

The present study has been focused on the working capital ratios impact on the financial performance of the organization with the help of secondary data. The study has considered the IT sector industries and collected the working capital financial key ratios from the period of 2016-17 to 2020-21 year. The study has considered the working capital key ratios with the operating profitability and the result stated that all the selected key ratios are having the significant relationship with the operating profitability. The Wipro should focus more on the asset turn over ratio, which will effect the ROTA positively. Hence there is a need to do research in this area by considering the industries fundamental key factors impact on the growth of the organization.

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