

A Study on Inventory and Cash Management of Small Enterprises Operating in Shillong City of Meghalaya

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Abstract

Small enterprises play a strategic role in restructuring and in transformation of an economy with a comparatively higher labour-capital ratio and a shorter gestation period. Every business concern needs working capital to run the day-to-day business activities. They also generate a lot of employment which have a far reaching effect on the community, state and national level as a whole and as a result of which there is a growth in the economy. The present study aims to analyse the management of inventory and cash of business units in Shillong city of Meghalaya. The study concludes that sample units do not use any effective tools for proper management of both cash and inventory and therefore, results are not satisfactory.

Key Words: *Small Enterprises Working capital, Inventory Management, Cash Management*

JEL Classification: *G31, D24*

Introduction

An efficient inventory and cash management plays a vital role in the development of economies of the enterprise as well as country. Every business concern needs working capital to run the day -to-day business activities. The micro and small scale industries in the state of Meghalaya have become very popular and providing a lot of services to the people of the community. They also generate a lot of employment which have a far reaching effect on the community, state and national level as a whole and as a result of which there is a growth in the economy. These industries provide a general framework for the variety of entrepreneurial ideas of the people. Small enterprises in Meghalaya are considered to be significant contributors to economic development.

The inefficient working capital management will lead to loss of profits in the short run but it will ultimately lead to the downfall of the enterprise in the long run. On the other hand, optimal level of working capital maximises firm value (Deloof, 2003). Therefore, the objective of working capital management is to keep balance of each component of working capital and try to obtain the optimal level of working capital in a firm (Fillbect & Krueger, 2005). Further, efficient working capital management signifies the uninterrupted movement of business cycle in respect of payment of liabilities and procurement of raw materials. Cash management helps in ensuring proper availability of cash and minimises the amount of idle cash. It also assists in optimising liquidity and profitability. The need to

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maintain effective working capital management within Small and Medium scale Industries remain pivotal to solvency and liquidity of SMEs (Sunday, 2010). On the other hand, proper inventory management looks into the aspects of optimisation of investment in inventory, avoid over stocking, regular monitoring of stock levels, availability of material in time, etc. Thus, an efficient management of inventory and cash are essential requirements for the success of a business unit.

Review of Literature

Majumdar (1992) studied the pattern of financing the corporate working capital in India. The study indicates that major share of working capital finance is from borrowings and the effect of cost on the selection of sources of working capital is not at all significant.

Vijaykumar & Venkatachalam (1996) analysed the performance of Tamilnadu Sugar Corporation for the period from 1985-86 to 1993-94. The study found that during the study period the corporation maintained moderate level of working capital, less amount from long term-funds had been used for meeting short-term liabilities and profitability was affected due to excess liquidity.

Vora (2009) studied the working capital management of thirty Trading Houses in India listed on Bombay Stock Exchange. The study suggested that the financial manager should determine the optimum level of current assets so that the wealth of shareholders is maximized.

Harif, Osman, & Hoe (2010) studied financial management practices of small and medium scale enterprises in Malaysia. The study found that lack of working capital is the most common weakness in the area of financial management.

Sunday (2010) found that most small and medium scale enterprises do not care about their working capital position, most have only little regard for their working capital position and most do not even have standard credit policy.

From the above review of literatures, it has been discovered that no studies have been carried out on Working Capital management of Small units or enterprises in Meghalaya. Most of the work has been done in the developed parts of the country and abroad. Therefore, an attempt has been made to make a comprehensive study on the Inventory and Cash management of some selected small enterprises in the city of Shillong, Meghalaya.

Objectives of the Study

1. To assess the inventory and cash management of select small enterprises operating in Shillong city of Meghalaya.
2. To analyse the efficiency in working capital management of select small enterprises operating in Shillong city of Meghalaya.

Methodology of the Study

Data of the Study: The study is based on both primary and secondary data. Primary data have been collected through questionnaire and face-to-face interview with entrepreneurs, officials, non-officials and other experts in the field. The sources of

Secondary Data for this study are financial reports of the industry published in Statistical hand book of Meghalaya for the period of five years from 2014-15 to 2018-19.

Locale of the Study: The study is confined to the city of Shillong, the capital city of Meghalaya and the fourth largest city in North East India (Census of India, 2011). The study has considered two wooden furniture making units (Group I) and two flour mills (Group II) registered as small scale industries in the Department of Industry and Commerce, Shillong, Meghalaya. All the units which were selected for the study are located in the Myllem Block of the East Khasi Hills District of Meghalaya.

Tools and Techniques of Analysis: The present study has adopted financial ratios, namely, Working Capital Turnover Ratio, Return on Total Assets, Inventory Turnover Ratio and Stock Velocity. Besides, Baumol's Cash Management Model has also been employed for analysing the management of cash. Arithmetic Mean, Standard Deviation and Coefficient of Variation have also been considered under the study.

Table 1: Concept of Ratios and Model used

Ratio	Definition	Formula
Working Capital Turnover Ratio	This ratio establishes the relationship between net working capital and cost of goods sold or net sales. It helps in judging the efficiency of working capital in an enterprise. The higher the ratio, the better is the financial position.	$\frac{\text{Net Sales or Cost of Sales}}{\text{Net Working Capital}}$
Inventory Turnover Ratio/ Stock Turnover Ratio	It establishes relationship between cost of goods sold during a given period and with the average amount of stock/ inventory carried during that given period. This ratio indicates the number of times stock is turned into sales during the accounting period. The higher the ratio, the better is the financial position of the concern.	$\frac{\text{Cost of Goods Sold}}{\text{Average Stock}}$
Return on Total Assets	This ratio helps in judging the overall efficiency and profitability of an enterprise. This is also good for inter- firm and intra-firm comparison.	$\frac{\text{Profit before Interest, Tax and Dividends}}{\text{Total Assets}}$
Stock Velocity	This tool is the ratio between total number of days or months or weeks in a particular year and the total inventory or stock turnover ratio.	$\frac{365 \text{ days}}{\text{Inventory Turnover Ratio}}$

William J Baumol's Cash Management Model	This model finds a correct balance by combining holding cost and transaction costs, so as to minimise the total cost of holding cash.	$C = \sqrt{\frac{2AT}{I}}$ where, C = Optimum level of cash balance estimated T = Cost per transaction of purchase and I = Interest on marketable securities
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Source: Review of existing literatures

Data Analysis

Table 2: Socio Economic Profile of Meghalaya

Area (in square kilometres)	22,429
Total Population	29,66,889
Rural	23,71,439
Urban	5,95,450
Population size : Male	14,91,832
Female	1,47,057

Source: Census of India, 2011

From the Table 2, it is found that total area of the Meghalaya is 22,429 square kilometres and the total population was 29,66,889 as per 2011 census. The rural population size was 23,71,439 and the urban population size of Meghalaya was 5,95,450. The population size of male was 14,91,832 and female was 1,47,057 as per 2011 census.

Table 3: Average Stock of select Small Scale Enterprises

(Figure in Rupees)

Units	Total average amount Spent on Inventory Yearly	Minimum Average Amount of stock kept Yearly	Maximum amount of stock kept Yearly	Average Stock
Group I	11,28,37,500	45,06,782	42,44,282	38,25,532
Group II	21,70,48,697	87,10,910	1,58,00,000	1,57,88,788

Source: Field Study

Table 3 presents average stock of select small scale enterprises during the study period. It can be observed from the table that the flour mills (Group II) have the highest amount of minimum, maximum and average stock and their total amount yearly spent on inventory was even much higher than the furniture making units (Group I).

Table 4: Placement of Order for Raw Materials

Particulars	Number of Units	Percentage
Weekly	02	50
Monthly	00	0
Daily	02	50
Fortnightly	00	0
Total	04	100

Source: Field Study

From Table 4, it is found that 50% of the units selected for the study place their order for raw materials weekly and the remaining 50% of the units place their order for raw materials daily while none of the units place order for raw materials monthly or fortnightly basis.

Table 5: Inventory/Stock Turnover Ratio of select Small Scale Enterprises

(Figure in times)

Units	2014-15	2015-16	2016-17	2017-18	2018-19	Mean	SD	CV (%)
Group I	7.73	6.57	7.13	8.91	9.27	7.78	1.04	13.34
Group II	16.92	17.07	17.81	18.53	19.12	17.89	0.84	4.72

Source: Based on data obtained from Statistical hand book of Meghalaya (Various Issues)

From Table 5, it can be observed that among all the units selected for the study, the mean value of flour mills (Group II) is much higher as compared to Group I. Further, the SD and CV of Group I is higher during the study period. This implies that the flour mills (Group II) have a sound financial position and the amount of risk taken on management of inventory is limited.

Table 6: Stock Velocity of select Small Scale Enterprises

(Figure in days)

Units	2014-15	2015-16	2016-17	2017-18	2018-19	Mean	SD	CV (%)
Group I	47.20	55.58	51.17	40.95	39.38	46.86	6.81	14.54
Group II	21.57	21.38	20.49	19.69	19.08	20.44	1.07	5.23

Source: Based on data obtained from Statistical hand book of Meghalaya (Various Issues)

Table 6 depicts group wise stock velocity of select small scale enterprises. It is found from the table that the stock velocity of the furniture making units is very much higher than the flour mills. It indicates that these units have a very low stock turnover ratio as a result of which their stock velocity is so high. Thus, it can be noted that if the inventory turnover ratio increases, the average age of inventory will go down and vice-versa. On the

other hand, the performance of flour mills is better than furniture making units in terms of consistency as evident from lower coefficient of variation.

Table 7: Awareness about the Baumol's Cash Management Model

Particulars	Frequency (No. of units)	Percentage
Extremely aware	0	0
Moderately aware	2	50
Not at all aware	2	50
Total	04	100

Source: Field Study

Table 7 shows the awareness of the respondents regarding the Baumol's Cash Management Model for cash management. It can be identified that none of the units adopt Baumol's cash management model for management of cash. However, 50% of the units selected under the study have some idea about Baumol's cash management model but did not adopted this method for the management of cash. Further, remaining 50% of the units do not have any idea about Baumol's cash management model for the management of cash.

Table 8: Optimum Cash Balance as per Boumol's Cash Management Model

(Figure in Rupees)

Units	2014-15	2015-16	2016-17	2017-18	2018-19	Mean	SD	CV (%)
Group I	38301.00	41935.60	40732.00	40354.20	42212.76	40707.11	1556.49	3.82
Group II	74230.16	71564.00	80560.18	83514.65	79337.06	77841.17	4854.41	6.24

Source: Based on data obtained from Statistical hand book of Meghalaya (Various Issues)

Table 8 presents the optimum level of cash balance of select small scale enterprises. Higher the optimum cash balance, better is the financial position and cash management. From the table, it is found that the flour mills have a higher optimum level of cash balance as compared to the furniture making units. It can be identified clearly that the optimum cash balance is fluctuating rapidly over the past five years.

Table 9: Working Capital Turnover Ratio of Select Small Scale Enterprises

(Figure in times)

Particulars	2014-15	2015-16	2016-17	2017-18	2018-19	Mean	SD	CV (%)
Group I	2.28	3.26	2.67	3.14	3.09	2.89	0.36	12.57
Group II	4.64	5.36	3.96	2.69	3.78	4.09	0.89	21.80

Source: Based on data obtained from Statistical hand book of Meghalaya (Various Issues)

From Table 9, it can be clearly stated that the flour mills have a higher working capital turnover ratio and a higher SD during the study. On the other hand, furniture units

have a lower working capital turnover ratio and also a lower SD. Moreover, the furniture making units also have a lower coefficient of variation which signifies that they initiate lower risk while performing their business operations as compared to the flour mills selected under the study.

Conclusion

To conclude that it is be stated that performance of the select units in respect of working capital management is not satisfactory as they do not use any effective tools for proper management of both inventory and cash. As a result of this, failure of most of the enterprises is a result of poor working capital management, poor management of inventory and cash as well. Thus, it is advisable to all the units under study to maintain a proper working capital management policy, which might enable them to run their business properly and meet their day-to-day business expenditure smoothly and efficiently, with a view to maintain a proper balance between liquidity and profitability in the long run.

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