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Assessing the Impact of Liquidity on Profitaility of Steel Companies with Special Reference to Sail (Steel Authority of India): The Financial Statement Analysis Approach

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Abstract - This paper assess the liquidity on profitability ratios of steel companies with special reference to SAIL (Steel Authority of India) of last 5 years i.e. 2016 to 2020. Liquidity ratio is used to judge the ability of a firm to meet its short term maturing obligations. The higher the ratio the greater the margin of safety for short term creditors. While profitability ratio is concerned with relative profitability and efficient utilization of resources of a business. Thus, this study seeks to determine the following: Correlation between Current ratio and profitability, as measured by the return on assets, the correlation between Acid test ratio and Profitability as measured by return on assets, the Correlation between Current ratio and Return on equity, the Correlation between Acid Test ratio and Return on equity, correlation between Current ratio and return on capital employed, correlation between Acid Test Ratio and Return on Capital Employed. Simple Correlation and Regression analysis was used to test the hypothesis at 5% level of significance. The findings of this study reveal that there is a high positive correlation between Current ratio and all dependent variables, and a very high positive correlation between Acid Test Ratio and all dependent variables. With the help of regression analysis, findings reveal that there is a approximate 56% impact of current ratio on dependent variables and there is a approximate 89% impact of Acid Test Ratio on dependent variables.

Keywords - Working Capital, Profitability, Liquidity

INTRODUCTION

Liquidity is very important factor in the business. Liquidity is very necessary for survival of business. Liquidity means the ability of a firm to meet its short term obligations. The firm should have to maintain balanced liquidity position which means that neither excess nor insufficient liquidity. The liquidity decision is one of the financial decisions in each organisation to maintain sufficient ability to meet its current financial obligations without any losses and interruption. The financial institutions are highly deal with ensuring adequate liquidity assets than non-financial institutions to meet the customer's demands to survive in competitive market successfully. In financial institutions, adequate liquidity means capacity of the institutions to convert their assets into cash to meet the needs of the customers wanting to withdraw funds, provide new loans demand and borrowers wanting to be assured that their credit or cash needs will be met.

Liquidity management is very important for every organization means to pay current obligations on business, the payment obligations including operating and financial expenses that are short term but maturing long term debt. Liquidity ratios are used for liquidity management in every organization in the form of current ratio and quick ratio that greatly affects the profitability of organization. So, business has enough liquid assets (Cash, Bank) to meet the payment schedule by comparing the cash and near cash with the payment of obligations. The near cash assets include receivables from customers and inventories of finished goods and raw materials. The payment obligations include dues to suppliers, operating and financial expenses that must be paid shortly and maturing installments under long term debt.

Indian steel Industry has made a rapid growth on strong fundamentals in the recent year. The industry is receiving almost all essential ingredients necessary for dynamic growth. The government is supporting the industry through the liberal industrial reforms, while the private sector is supporting it with investments worth billions of dollars. The new economic policy initiated in 1990 has influenced Indian iron and steel industry in many ways. For steel makers, economic reforms opened up new channels for their inputs at competitive prices from the overseas market while unveiling the new markets for their products.

Steel is the most important multi-functional and adaptable material. Steel as compared to other materials it has a low production cost. It is environment friendly as can be recycled. Steel production is twenty times higher as compared to production of all non-ferrous metals put together. Due to it's this feature country focus on these industry.

SAIL, one of the leading steel making company in India. It entirely integrated to iron and steel production; it produces both basic as well as special steels for domestic construction, engineering, power, railway, automotive, defence industries and for sale in the export market. Among the central public sector enterprises, SAIL is one of the seven Maharatna of central public sector enterprises of the country along with CIL, IOCL, NTPC, BHEL, GAIL and ONGC. The government of India owns 75% of the SAILs equity and retains voting control of the company. Its annual turnover for year 2015-16 is 43.337 crore. As SAIL is one of the Maharatna Company, it enjoys significant operational and financial autonomy.

The researcher has formulated below mentioned ratios to analyze liquidity and profitability of Steel Authority of India:-

(1) Current Ratio: Current Assets/Current Liabilities

(2) Quick Ratio/ Acid Test Ratio/ Liquid Ratio: Current Assets- Inventory- Prepaid Expenses/ Current Liabilities

(3) Return on Assets: Net Income/ Total Assets

(4) Return on Equity: Net Income/ Shareholder's Equity

LITERATURE REVIEW

Rafiq Ahmad (2016), has measured the relationship between the two ratios i.e. profitability and liquidity of Standard chartered Bank Pakistan. The relationship is measured by current ratio, quick ratio and net working capital. The findings of this study are that there is a positive relation between profitability and liquidity and there is a positive relationship between net working capital and profitability.

Jalpa.H. Panrey (2015), has done analytical study of liquidity in oil and gas refineries in India i.e. IOC, ONGC, HPCL, BPCL for the period of 5 years. Researcher has used various accounting ratios and F-test one way ANNOVA table as a statistical tool for data analysis. The main purpose of research work is to measure liquidity position and get idea about financial health and solvency of selected oil and gas refineries in India. The findings of this study reveals that positions of both the ratios are average but not sound except ONGC.

Mohammad Yameen (2019), has investigated the impact of liquidity on profitability of pharmaceutical companies listed on Bombay stock exchange (BSE). The analysis is done using a balanced panel data of 82 pharmaceutical companies for the period of 10 years. This research reveals that current liquidity ratio and quick ratio have a positive and significant impact on the profitability of pharmaceutical sector measured by return on assets, while the control variables have a negative impact on the profitability of pharmaceutical companies.

Pokharel Shiva Prasad (2019), has explores the influence of liquidity on the profitability in the Nepalese Commercial Banks in Nepal i.e. Agriculture Development Bank, Everest Bank, Prime commercial bank, Sunrise bank and Citizens Bank International are randomly selected among 28 commercial banks. The research concluded that bank's liquidity ratios have below the prescribed standard. The CRR and IGSCA are positively correlated with ROA while CRR and CBBISD are inversely correlated with ROA. There is a significant relationship between liquidity ratios with profitability except between IGSCA and ROA.

OBJECTIVES OF THE STUDY

A. To make analysis of liquidity position of Steel Authority of India.

B. To measure the impact of liquidity on the profitability of Steel Authority of India by using liquidity ratios.

PERIOD OF STUDY

The present study has been made on the basis of financial data for the period of last five years i.e. year 2016 to 2020 of the Steel Authority of India.

SOURCES OF DATA COLLECTION

The Present research study is mainly based on the secondary data collected from the Annual Report of Steel Authority of India. Researcher has used various newspapers, magazines and websites for better reliability and authenticity.

HYPOTHESIS OF THE STUDY

H_0: There is no positive relation between the current ratio and profitability i.e. return on assets.

H_0: There is no positive relation between the current ratio and profitability i.e. return on equity.

H_0: There is no positive relation between the current ratio and profitability i.e. return on capital employed.

H_0: There is no positive relation between the Quick ratio and profitability i.e. return on assets.

H_0: There is no positive relation between the Quick ratio and profitability i.e. return on equity.

H_0: There is no positive relation between the Quick ratio and profitability i.e. return on capital employed.

H_1: Current Ratio is positively correlated with profitability i.e. on Return on Assets (ROA).

H_2: Quick Ratio is positively correlated with profitability i.e. on Return on Assets (ROA).

H_3: Current Ratio is positively correlated with profitability i.e. on Return on Equity (ROE).

H_4: Quick Ratio is positively correlated with profitability i.e. on Return on Equity (ROE).

H_5: Current Ratio is positively correlated with profitability i.e. on Return on Capital Employed.

H_6: Quick Ratio is positively correlated with profitability i.e. on Return on Capital Employed.

LIQUIDITY AND PROFITAFILITY RATIOS OF STEEL AUTHORITY OF INDIA (SAIL)

Ratios/ Year	**2016**	**2017**	**2018**	**2019**	**2020**
Current Ratio	0.62	0.55	0.68	0.77	0.91
Quick Ratio	0.24	0.21	0.29	0.38	0.38
Return on Assets	-4	-2.65	-0.42	1.87	1.61
Return on Equity	-10.25	-7.86	-1.34	5.71	5.08
Return on Capital Employed	-7.63	-3.49	2.87	9.19	9.26

CORRELATION AND REGRESSION

	CORRELATION	REGRESSION
Current Ratio and Return on Assets	0.741	0.549
Current Ratio and Return on Equity	0.768	0.59
Current Ratio and Return on capital employed	0.76	0.578
Acid Test Ratio and Return on Assets	0.939	0.882
Acid Test Ratio and Return on Equity	0.963	0.927
Acid Test Ratio and Return on Capital Employed	0.937	0.878

CONCLUSION

The impact of liquidity has been studied many a times on profitability, but this study brings the impact of liquidity on profitability of Steel Companies with special reference to SAIL (Steel Authority of India) for the period of five years from 2016 to 2020. For assessing the relationship between liquidity and profitability, different ratios i.e. current ratio, Acid test ratio, Return on Assets, Return on Equity and return on capital employed and different statistical tools like Correlation, regression have been used for assessing the impact of liquidity on profitability. From 2016 to 2020 the current ratio and acid test ratio is improving but the company needs to maintain more current or liquid assets for maintaining good working capital condition. Return of Assets is improving year to year but it is very low which means the company is not earning enough as amount of investment. Return of equity has been improved from 2016 to 2020 but it is less than ideal ratio which means they need to improve their financial performance. Return on capital employed has improved from 2016 to 2020. The findings also reveals that there is a high positive correlation between independent variable i.e. current ratio and all dependent variables i.e. return on equity, return on assets & return on capital employed and a very high positive correlation between independent variable i.e. acid test ratio and all dependent variables i.e. return on equity, return on assets & return on capital employed.

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