EFFECTIVE CAPITAL MANAGEMENT: TOOL FOR ORGANIZATIONAL GROWTH A SURVEY OF SELECTED MANUFACTURING FIRMS IN DELTA STATE, NIGERIA

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Abstract
The study investigated effective working capital management, tool for organizational survival. The study spotlighted the concept of working capital, factors that influence the working capital requirements of firms and the symptoms of shortage of working capital and under capital. Structured questionnaire was employed in the course of gathering relevant data for the study and administered on 80 employees of the organizations under study in Delta State. Data analysis was made using simple percentage tables. The hypotheses formulated were tested using chi-square test ($X^2$) statistical technique at 0.05 level of significance. The results showed that there is positive relationship between effective working capital management and management of inadequate and surplus working capital. The study concludes that effective working capital management minimize the effect of overtrading and undertrading. The study, however, recommended proper management of trade creditors, trade debtors and inventories for effective working capital management in organizations.

Keywords: Working Capital; Management; Tool; Organizations; Survival

Introduction
Working capital is the excess of current assets over current liabilities. This is what is referred to in the balance sheet as the net current assets. Working capital therefore represents the funds used to finance production such as the purchase of raw materials, to finance inventories and provide credit to customers. For example, a firm that does not enjoy credit from its suppliers of goods and services would have to raise funds to purchase raw materials, pay salaries and other production overhead costs until the raw material undergo all the manufacturing process and then become finished goods to be sold. The funds so used until money comes in from the sales of the finished products, is part of the firms working capital. Also, if some of the sales are in credit. It means that the firm will have to raise additional working capital equivalent to the credit sales for the period of the credit given to customers to pay for raw materials, salaries and other costs. This will result in an increase in the working capital. however, the amount of working capital required would decrease if raw materials could be obtained on credit by the amount of credit given.

The research hypotheses formulated in the null form for this study would be tested and they are firstly, effective working capital management has no significant relationship with management of
inadequate working capital in organizations and secondly, there is no significant relationship
between effective working capital management and management of surplus working capital.

Working capital management is therefore the administration of the company’s current assets and
the financing need to support these current assets. It can also be viewed as the balancing the
liquidity and profitability objectives of the company as well as taking cognizance of the risk.

Akinsulire (2006) views working capital management as the management of all aspects of current
assets and current liabilities. Thus working capital management simply means management of
cash, management of debtors, management of stock and management of creditors.

The management of the various components of working capital involves determining the optimal
level of which the controllable ones should be maintained at a particular time, level of funds that
the management is ready to allocate to the different forms of current assets, how the current assets
should be financed e.g. short or long term and the relationship between levels of fixed assets and
current assets (Akinsulire, 2006).

Shiro (2004) defines working capital as the capital available for the day-to-day running of an
organization or business enterprise.

Ovuielefuoma (1993) listed some factors which generally influence the working capital
requirements of the firm to include:

- **Production cycle**: Production cycle commences with procurements and use of raw
  materials and completes with the production of finished goods. The longer the production
  cycle, the larger the working capital requirement

- **Nature of business**: The nature of the business has substantial influence on working capital
  requirements. Trading companies have very little investment in fixed assets relative to the
  amount required for working capital investment.

- **Size of business**: The size of the business also plays an important role on working capital
  requirements. Size may be measured in terms of scale of operation. As the scale of
  operation increases, there will be need to build up additional raw materials to meet higher
  production requirements, additional debtors arising from the additional sales and additional
  finished goods to satisfy higher sales demand.

- **Business fluctuations**: Most companies experience seasonal and cyclical fluctuations in
  the demand for their products and services. These business variations affect the working
  capital requirements. Under boom, companies will usually increase the scale of operation
  necessitating additional investment in both fixed and current assets consequently, under
  trade recession, sales will fall and consequently, the levels of stocks and debtors will also
  fall.

- **Credit policy**: The credit policy of the company affects working capital by influencing the
  level of debtors. A liberal credit policy is expected to lead to high investment in debtors
  and by extension a higher working capital requirement.

- **Availability of credit**: The working capital requirement of a company is also largely
  affected by credit terms granted by its creditors. Less working capital will be required by
  a company that enjoys liberal credit terms from his suppliers. Besides, a company, which
can get bank credit easily on favourable conditions, will operate with less working capital than a company without such a facility.

- **Dividend policy:** The dividend policy of a company also influences the working capital requirements. Payment of dividend consumes cash thus, reduces company’s working capital to that extent. If the profits are retained in the business, the company’s working capital position will be strengthened.

- **Operating efficiency:** The operating efficiency of a company relates to the optimum utilization of resources at minimum costs. The company will be effectively contributing to its working capital if it is efficient in controlling the operating costs. The use of working capital is improved and pace of cash cycle is accelerated with operating efficiency, better utilization of resources improves profits ability and thus, helps in releasing pressure on working capital.

- **Price change:** General rising price level will require a company to maintain higher amount of working capital. The same levels of current assets will need increased investment when prices are increasing.

The symptoms of shortage of working capital are: A low average collection period; high stock turnover; a rapid growth in current assets; a low liquidity ratio; significant increase in overhead costs which may lead to fall in net profit margin; if it is a listed company, its shares price will drop, as prospective investors will be unwilling to buy the shares; the firm will not be able to settle suppliers promptly resulting loss of discount revenue, the firm may miss profitable opportunities due to shortages of liquid resources (Aborode, 2005; Akinsulire, 2006; Ovwielefuoma, 1993 and Shiro, 2004).

The symptoms of excessive working capital are high liquidity ratios; low stock turnover; high average collection period; low creditors payment period; losses of interest on capital tie down unnecessarily; it results in unnecessarily accumulation of inventories, thus chances of inventory mishandling, waste, theft and losses increase (Shiro, 2004; Aborode, 2005; Akinsulire, 2002 and Ovwielefuoma, 1993).

**Materials and Methods**
Research questionnaire designed and administered on 90 respondents of the six organizations under study in Delta State. The secondary data were obtained from textbooks. The methods of data analysis include tables, simple percentages and chi-square ($X^2$) statistical technique was used to test the hypotheses formulated and whose function is:

\[ X^2 = \sum \frac{(fo - fe)^2}{fe} \]

Where, $X^2$ = Chi-square  
   fo = Observed frequency  
   fe = Expected frequency  
   $\sum$ = Summation sign

**Results and Discussion**
The tables presented below contain the analytical details relating to my findings from the respondents.
Table 1: Manufacturing firms studied with number of respondents in Delta State

<table>
<thead>
<tr>
<th>S/N</th>
<th>Manufacturing Organizations</th>
<th>No. of Respondents</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>Vita Foam Plc, Sapele</td>
<td>20</td>
</tr>
<tr>
<td>2.</td>
<td>Imoniyame Rubber Holding Ltd, Ughelli</td>
<td>20</td>
</tr>
<tr>
<td>3.</td>
<td>Beta Glass Plc, Ughelli</td>
<td>20</td>
</tr>
<tr>
<td>4.</td>
<td>Industrial Gas Ltd, Warri</td>
<td>10</td>
</tr>
<tr>
<td>5.</td>
<td>Eternit Nigeria Plc, Sapele</td>
<td>5</td>
</tr>
<tr>
<td></td>
<td><strong>Total</strong></td>
<td><strong>80</strong></td>
</tr>
</tbody>
</table>

Source: Research Data, 2016

Table 2: Working capital management and its significant relationship with management of inadequate working capital

<table>
<thead>
<tr>
<th>Responses</th>
<th>Frequency of Occurrence</th>
<th>Percentage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>77</td>
<td>96.25</td>
</tr>
<tr>
<td>No</td>
<td>3</td>
<td>3.75</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>80</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Source: Field Work, 2016

Table 2 above shows that seventy-seven (77) respondents are of the view that effective working capital management has significant relationship with management of inadequate working capital in the organizations under study. The respondents stood for “Yes” at 96.25% while three (3) respondents stood against “No” at 3.75%.

Table 3: Working capital management and its significant relationship with management of surplus working capital

<table>
<thead>
<tr>
<th>Responses</th>
<th>Frequency of Occurrence</th>
<th>Percentage (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>78</td>
<td>97.5</td>
</tr>
<tr>
<td>No</td>
<td>2</td>
<td>2.5</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>80</strong></td>
<td><strong>100</strong></td>
</tr>
</tbody>
</table>

Source: Field Work, 2016

Table 3 reveals that seventy-eight (78) respondents agreed that effective management of working capital has significant relationship with management of surplus working capital in the firms under study. The respondents stood for “Yes” at 97.5% against “No” at 2.5%.

Table 4: Chi-square data and statistical computation

<table>
<thead>
<tr>
<th>Responses</th>
<th>Observed Frequency (fo)</th>
<th>Expected Frequency (fe)</th>
<th>fo – fe</th>
<th>(fo – fe)² / fe</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>77</td>
<td>40</td>
<td>37</td>
<td>34.22</td>
</tr>
<tr>
<td>No</td>
<td>3</td>
<td>40</td>
<td>-37</td>
<td>34.22</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>80</strong></td>
<td><strong>80</strong></td>
<td>-</td>
<td><strong>68.44</strong></td>
</tr>
</tbody>
</table>

Source: Research Data, 2016 (Drawn from table 2)

Table 4 above, the calculated $X^2$ is 68.44 and is greater than the $X^2$ table value of 3.841. The null hypothesis is therefore rejected. It indicates therefore, that there is significant relationship between effective working capital management and management of inadequate working capital in the organizations under study. Working capital if effectively managed, will result in organizations been able to settle suppliers promptly resulting in gain of discount revenue, it will result in preventing
unnecessary pressure exerted on customers for the payment of their debts; the firm may gain profitable opportunities due to adequate liquid resources if it is a listed company, its share prices will increase, as prospective investors will be willing to buy the shares and the firm will gain its reputation when it is in position to honour its short-term obligations.

Table 5: Chi-square data and statistical computation

<table>
<thead>
<tr>
<th>Responses</th>
<th>Observed Frequency (fo)</th>
<th>Expected Frequency (fe)</th>
<th>(fo – fe)</th>
<th>(fo – fe)^2</th>
<th>(\frac{(fo – fe)^2}{fe})</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
<td>78</td>
<td>40</td>
<td>38</td>
<td>36.1</td>
<td></td>
</tr>
<tr>
<td>No</td>
<td>2</td>
<td>40</td>
<td>-38</td>
<td>36.1</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>80</td>
<td>80</td>
<td>-</td>
<td>72.2</td>
<td></td>
</tr>
</tbody>
</table>

Source: Research Data, 2015 (Drawn from table 3)

Table 5 above, the calculated \(X^2\) is 72.2 and is greater than the \(X^2\) table value of 3.841. The null hypothesis is therefore rejected. Thus, effective working capital has significant relationship with management of surplus working capital in the organization under study. Working capital if effectively managed, will prevent unnecessary accumulation of inventories. Thus, chances of inventory mishandling, waste, theft and losses will decrease, losses of interest on capital tie down will be minimized, higher incidence of bad debts will not arise and this will improve profitability.

Conclusion and Recommendations

This study aims at examining the imperatives of effective working capital management: tool for organizational survival and proffered solutions for effective management of working capital in organizations. From the study, it suffice to conclude that effective working capital management in organizations minimize the effect of overtrading and undertradings.

The following strategies are recommended based on the findings and conclusions of this study for effective working capital management in organizations.

1. **Management of trade debtors:** Management of trade debtors requires experience, an in-depth appraisal of the prospective buyers and the credit terms offered by its competitors for a firm to be able to establish a sound credit policy. In establishing a sound policy on trade debtors management, management should consider cash discount, length of credit period, credit worthiness of the customers and action to be taken regarding late payment.

2. **Cash management:** The importance of proper cash management cannot be over-emphasized. A highly profitable project can be seriously impeded if cash is not available at the appropriate time to pay for necessary supplies. On the other hand, if the business is carrying too much cash balance, that is an indication that the resources of the business are being wasted. Unfortunately, such a business will not earn sufficient return relative to the capital employed for its resources.

3. **Proper management of trade creditors:** Trade credit is an important source of short term financing. The longer the credit period obtained from suppliers, the less the amount of working capital required.

4. **Proper management of inventories or stocks:** Inventory or stock consists of finished goods, work in progress and raw materials. The guiding principle of firms is that its stock levels should be optimal, it should not be neither too large nor too small. If stock is too large excess capital will be tied up in stock unproductively, cost of storage (e.g. insurance and warehousing) will rise and there is the risk of deterioration and obsolescence due to
the length of time in storage. On the other hand, if it is too low, production may be interrupted due to shortage of stock, frequent ordering will result in increase in ordering costs while the discount on the purchase of large quantity will be lost.

References


