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Analysis Working Capital on Company Profitability

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ABSTRACT

Working capital required for business continuity of a company. Profitability is the company's ability to generate profit in one period. Factors that affect the profitability is working capital. This research aims to determine the effect of working capital on the company's profitability. Working capital will be calculated using the WCT (Working Capital Turn offer), while profitability will be calculated using ROA (Return on Assets). The populations in this study were all Food and Beverages company in The Indonesia Stock Exchange. The data used in this research is the documentation of data, using purposive sampling in getting the data. The data of this study from 2008 to 2012 as many as 70 data of the company. The result of this research shows that working capital positively and significantly the profitability. Working capital management Efficient will have an impact on profitability. The Company to maintain Working capital to the optimal amount that of capital can't unemployed and be invested in other forms that can increase profitability.

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INTRODUCTION

This paper investigates analysis working capital on company profitability for a sample of 70 data Indonesia Food and Beverages companies listed on the Indonesia Stock Exchange for the period of 5 years from 2008 – 20012. In running the operating companies in need of funds, the Fund may be obtained from the owner of the company or a debt from creditors. Funds received are used for the operations of the company. Working capital required for business continuity of a company. Financial capital is an essential tool in any sustainable business but the peculiar nature of Insurance business position capital more in the context of underwriting capacity. However, despite increase in the emergence of business opportunities and clients due to technology's improvement, availability and increasing adoption rate, there are countless challenges in the undertaking and successfully execution of feasible business due to inadequate capital required to exploit the various opportunity in the environment (Abdurahmon Onaolapo, 2012). Errors in managing working capital resulted in business activities can be inhibited or stopped altogether, otherwise excessive working capital indicates that funds are not productive, This will result in losses for the company, because of the capacity that is not used so that the opportunity to benefit squandered. Profitability is the ability of the company makes a profit in a given period. Good management of working capital, the company will bring benefit.

It seems that operational profitability dictates how managers act in terms of managing accounts receivables. Thus, the findings of this paper suggest that managers can create value for their shareholders by reducing the number of days for accounts receivables. In addition, the negative relationship between accounts receivables and firm's profitability suggest that less profitable firms will pursue a decrease of their accounts receivables in an attempt to reduce their cash gap in the cash conversion cycle. On the basis of findings of this paper, we conclude that profitability can be enhanced if firms manage their working capital in a more efficient way (Amarjit Gill, 2010). Management of working capital is an important component of corporate financial management because it directly affects the profitability of the firms. Management of working capital refers to management of current assets and of current liabilities (Garcia–Teruel, 2007; Besley, 1987). While some studied the impact of proper or optimal inventory management, others studied the management of accounts receivables trying to postulate an optimal way policy that leads to profit maximization (Lazaridis Tryfonidis, 2006). According to Deloof the way that working capital is managed has a significant impact on profitability of firms. Such results indicate that there is a certain

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level of working capital requirement, which potentially maximizes returns (Deloof, 2003).

Firms may have an optimal level of working capital that maximizes their value. Large inventory and generous trade credit policy may lead to high sales. The larger inventory also reduces the risk of a stock-out. Trade credit may stimulate sales because it allows a firm to access product quality before paying (Raheman, 2007; Lina Warrad, 2013). Working capital is one of the vital decisions of financial management function. Profitability and working capital relationship is frequently emphasized for deciding on the level of investment in working capital. All manufacturing firms need to understand the association between these two variables to arrive at optimal financial decisions (Satyanarayana Chary, 2011).

Methodology:

This research uses SPSS regression for analysis and the data are the entire annual financial statement data *Food and Beverages* publicly traded companies as listed on the Indonesian Stock Exchange (BEI) in 2008-2014. There are 70 data used in this research. The data used in this research is the documentation of data, using purposive sampling in getting the data. The independent variable is Working capital using the proxy WCT (Working Capital Turn offer), and the dependent variable in the form of Profitability using the proxy ROA (Return on Assets).

Here is the formula ROA and WTC:

$$ROA = \frac{\text{Net profit after interest and tax}}{\text{total assets}}$$

$$WTC = \frac{\text{sales}}{\text{current assets - current liabilities}}$$

Regression equation in this research as follows:

$Y = \alpha + b_1 x_1 + e$

Specification:

Y = Profitability

α = constant regression equation

b_1 = regression coefficient

x_1 = Working Capital

e = standard error

Table 1: Descriptive Statistics

Variables	N	Minimum	Maximum	Mean	Std. Deviation
ROA	70	-1,07	5,15	0,1485	0,62906
WTC	70	0,56	42,23	7,6291	8,30010

Table 2: Testing the path coefficient.

Exogenous Variable	Endogenous Variable	Estimation Coefficient	t-statistic	*p-value*	Description
Working Capital Turn offer	Return on Assets	0,435	3,984	0,000	Significant

RESULTS AND DISCUSSIONS

As the above evidence, the results of hypothesis testing, by specifying relationships between variables in this model shows also the significance test by comparing the p-value with α (alpha). In fact, it produces endogenous variable Return on Assets that can be significantly explained by exogenous Working Capital Turn offer. The effect of Working Capital Turn offer on the Return on Assets is significant as p-value < 0,05. This research produces the p-value of 0,000 so that it is appropriate for the criteria in which it must be significant when it is less than 0,05, with a path coefficient of 0,435.

The path coefficients have the sense that every single unit of the relative variable of Working Capital Turn offer increases indicating that the Working Capital Turn offer variable is increased by 0.435. The findings of this study stated that Working Capital Turn offer has a positive effect on the Return on Assets. This also means that applying the Working Capital Turn offer in the cooperative will affect the Return on Assets. Thus, the better the Working Capital Turn offer the better the Return on Assets. In that condition, the control environment is the foundation for implementing Working Capital Turn offer in the Company.

The result of this research shows that Working Capital, positively and significantly, the Profitability. Sufficient working capital to enable the company to operate as economical as possible and the company will not have trouble or face the dangers that may arise due to the crisis or financial chaos. Working capital used to meet the liquidity needs of the company, with sufficient working capital the company has the ability to meet obligations. Profitability of a company is a reflection of the ability of the relevant company's capital for profit. Profitability is a reflection of a company's efficiency in the use of working capital. Capital is a tool with enough potential to improve the productivity, effectiveness and efficiency of the organization; implore communication and overall realization of objectives (Abdurahmon Onaolapo, 2012).

This research supports the research conducted the result that a significant impact of working capital turnover on profitability presented by return on assets of 11 Chemical Industries companies listed on Amman Stock Exchange covering the period from 2009 to 2011, (Lina Warrad, 2013). The study results approved the results of some previous studies such as (Arshad, 2013; Manzoor, 2013) study which revealed a significant negative effect of working capital on their firms' profitability. Also (Azam, 2011; Rahman, 2011) study those revealed a significant positive impact of working capital turnover on profitability. In general most previous studies proved the existence of impact of working capital turnover on profitability whether positive or negative and these results compatible with the study result.

Amarjit and Neil found that a negative relationship between profitability (measured through gross operating profit) and average days of accounts receivable and a positive relationship between cash conversion cycle and profitability (Amarjit Gill, 2010). Regarding the average days of accounts payable previous studies reported negative correlation of this variable and the profitability of the firm (Lazaridis Tryfonidis, 2006; Raheman, 2007; Garcia–Teruel, 2007). We found no statistically significant relationship between these variables. Examining the relationship between the average number of days the inventory is held and the profitability, Raheman and Nasr (Raheman, 2007) and Lazaridis and Tryfonidis (Lazaridis Tryfonidis, 2006) found that the relationship is negative.

Summary:

The result of this research shows that working capital, positively and significantly the profitability. Working capital used to meet the liquidity needs of the company, with sufficient working capital the company has the ability to meet obligations. Profitability of a company is a reflection of the ability of the relevant company's capital for profit. Working capital management Efficient will have an impact on profitability. The Company to maintain Working capital to the optimal amount that of capital can't unemployed and be invested in other forms that can increase profitability.

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