Chapter - IX

SUMMARY OF FINDINGS AND SUGGESTIONS
Introduction

In the foregoing chapters of this study an attempt has been made to study all aspects of its financial management in cotton mills i.e. fixed assets management, inventory management, cash management and evaluation of profitability. In this final and concluding chapter, the main lines of the argument developed are summarized and some practical suggestions are offered to better the financial management in cotton mills. A sample of four cotton mills in Telangana region, one cotton mill in Andhra region and one cotton mill in Rayalaseema region were selected for the present study. The data for the present study was collected directly from cotton mills concerned using a structured comprehensive schedule and also from secondary source. The data was tabulated and analysed thoroughly using appropriate techniques like ratios, averages, percentages and funds flow statements.

This study has brought to light the inadequacies of financial performance in cotton mills and provided empirical basis for offering specific suggestions for improving financial performance in cotton mills in Andhra Pradesh.

An overview of the cotton industry

The cotton textile industry is one of the oldest and major consumer goods industries in India. The industry produces a wide range of fabrics to suit specific needs and variegated tastes of the consumers. The largest share of all textile production goes to garment manufacture to readymade wear. The second largest share is used to make house hold product draperies, blankets, bed-sheets and towels. Textiles are also used to make varieties of products like, basket ball nets, boat sails, book binding, conveyor belts, fire houses, flags insulation materials, parachutes, type writing ribbons, umbrella, etc. Textiles are also used to make the products like adhesive types, bandages, surgical threads etc. used in hospitals.

M/s Ferguson and company started the first cotton mill in India known by Bouriah Mill in Calcutta in 1817. The second mill known Fort Glouster Mills was started in 1829 in Calcutta. These turned out to be unsuccessful. The spinning mill was set up by C.N.Devar in 1954 at Bombay followed by several mills at Ahmedabad and later in Kanpur, Madurai and Coimbatore. At the end of 1947, there were 423 mills with 103.54-lakh spindles and 2.03 lakh looms available in India.
The causes for fast development of cotton textile in Bombay before independence are cheap labour, warm climate and availability of raw cotton at cheap rate, abundance of coal, facilities for transit and capital sources.

In India, cotton occupies an area of nearly 7.39 million hectares with a production of 2.38 million metric tonnes (2002-03), ranking third in the world. The lint productivity of cotton is 322 kg/ha. During the last sixty years, production of cotton rose from 30 lakh bales (1 bales = 170 kg) in 1950-51 to 339 lakh bales in 2010-11. During the same period the area under cultivation increased from 58.82 lakh hectares to 111.42 lakh hectares. The cotton production in the country has touched an all time high during 2004-05 with a record production of 243.0 lakh bales (1 bale = 170 kg). The productivity of cotton has also shown significant growth with 463 kg/ha during 2004-05 compared to 399 kg/ha during 2003-04 when the production was 179 bales.

The cotton industry has been experiencing a severe setback during the last few years from the point of view of lower capacity utilization and lower profit earnings. The causes being the quality cotton shortage, cotton controls and levy, labour unrest, power handicaps and lot of price fluctuations in cotton. Besides, more often the industry has been facing odds and crises due to imprudent financial management. With a view to assessing the financial performance of cotton industry in Andhra Pradesh an empirical evaluation has been made to study the working of cotton mills during the period of 2001-02 – 2010-11.

Six cotton mills were selected for this study by adopting stratified random sampling technique. They are (1) Suryalatha spinning mills Ltd (2) Suryalakshmi cotton mills Ltd (3) Suryajyothi spinning mills Ltd (4) Suryavanshi spinning mills Ltd in Telangana region, (5) Sree Akkamamba Textiles Ltd in Andhra region, and (6) Pioneer spinning and weaving mills Ltd in Rayalaseema region.

The concept of financial management

Financial Management is a primary functional area of business management. It is concerned with raising of funds and their effective utilization. It involves planning and control of the funds through accounting and quantitative techniques in order to achieve the objectives of a business undertaking.
The objectives of any business undertaking are maximization of profits, maximization of wealth to shareholders, optimization of operational efficiency, maximization of sales and welfare of the employers. The primary objective of an undertaking depends upon the motive of investment which is to get highest returns on investment as well as enjoy the benefit of highest market value of the security. On the other hand, if the motive of investment is the welfare of the society at large or passing on higher economic benefit to the members, it should have optimization of operational efficiency. Accordingly wealth maximization is an appropriate objective for private sector undertakings. Whereas optimization of operational efficiency is an important objective for co-operative and public sector undertakings.

In order to achieve the enterprises objectives, financial manager has to perform certain tasks viz., (1) Financial forecasting, planning and control, (2) raising, investing and managing of funds, (3) measuring and controlling the cost of funds and (4) inventory management and evaluation of profits.

**Fixed assets management**

Investment on fixed assets is a capital expenditure. Decision making, planning and controlling investment on tangible assets with long life may be defined as fixed assets management. The profitability of an undertaking depends upon various factors of which utilization of fixed assets is one of the important factors. The higher the utilization of fixed assets, the higher will be the profit. So proper care should be taken in selecting investment proposals. Moreover, the selection of proper investment proposals is very significant because of two factors, viz, inflexibility and uncertainty.

One of the important aspects to be considered while taking investment decision is the source of finance. In order to maintain liquidity and solvency in business undertaking, it is better to finance fixed assets from long-term funds. The overall and individual structure and growth of fixed assets, the financing pattern of fixed assets, utilization of fixed assets, investment in fixed assets, and individual fixed assets have been discussed in fixed assets management chapter.
In the study of industry the investment in fixed assets was planned and controlled through capital budgeting technique. The first step in capital budgeting was evaluating and ranking investment proposals. There are three methods for evaluating and ranking investment proposals: (1). Pay-back period, (2) Rate of return method and (3) Discounted cash flow method. After the evaluation of the proposals, the investment decision on fixed assets is made with reference to the cost of capital. Any investment proposal with a rate of return below the cost of capital reduces the market value of the firm, hence it should be rejected.

The profitability of an undertaking depends on the efficiency and utilization of fixed assets. The higher the utilization of fixed assets the higher may be the profitability. West Wick has suggested the application of fixed assets turnover ratio to measure the assets utilization. The formula for finding fixed assets turnover ratio is

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\text{Fixed assets turnover ratio} = \frac{\text{Sales}}{\text{Fixed assets}}
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The value of fixed assets shows an increasing trend during the study period. On an average the fixed assets to total assets in Telangana region was 66.35 percent. The total average in Andhra region it was 73.10 percent and in Rayalaseema region it is 40.34 percent. The cotton mills provided depreciation every year. But the arrears of depreciation of fixed assets have been carried forward under section 205 of the Companies Act. The norms of fixed assets utilization will be at about 5 times in the fixed assets turnover ratio, but the average fixed assets turnover ratio in Telangana region was 2.11 times, 1.80 times in Andhra region and 5.63 times in Rayalaseema region. In the case of Rayalaseema region cotton mills the ratio was higher than the standard norm i.e. 5 times. This shows a very good performance in Rayalaseema region.

Fixed assets in cotton mills in the study include plant and machinery, land and buildings, vehicles and other fixed assets. The heavy outlay required while purchasing/constructing these fixed assets deserves careful consideration. The sample cotton mills adopted different policies to purchase/construct of fixed assets. Out of six mills, Suryalatha spinning mills Ltd have adopted the open tender system. The Pioneer spinning & weaving mills Ltd followed their own policies.
Suggestions

The following suggestions are made based on the findings drawn on fixed assets management. Investment in fixed assets is to be made from the ownership and long-term funds. All the Telangana, Andhra and Rayalaseema region cotton mills expanded their installed capacity in a significant manner because these mills had a reasonable margin in long-term funds to meet the permanent assets so as to enable them to enjoy the economics of scale.

Fixed assets should be utilized more effectively so as to produce more sales because the quantum of sales depends upon the size of investments in fixed assets. At present the size of investment in fixed assets is at satisfactory level in Telangana and Andhra region. But in Rayalaseema region it is very poor. As far as concerned to fixed assets turnover ratio Rayalaseema region cotton mill has more than the standard ratio i.e. 5:1 but in Telangana and Andhra region cotton mills never achieved standard ratio during the study period.

Inventory management

Inventory constitutes the largest component of current assets in most of the enterprises and therefore it occupies a key position in the financial management. Under investment as well as over investment in inventory affects the earning capacity of the undertaking. Proper management and control of inventory not only solves the acute problem of liquidity and profitability but also causes substantial reduction in the working capital of a firm. Inventory involves financial cost and maintenance cost. Inventories are operating assets bought with funds raised from some sources. Borrowing from commercial banks may mean a heavy interest burden. Therefore the financial manager, after considering the various aspects of this cost burden of inventory, has to decide the level of inventory to be ordered. Inventory management objective can be spelt out as the avoidance of over investment or under investment in inventories as an essential step to improve profitability. This can be achieved through proper inventory control system.
The important components of inventory in select cotton mills in the study are raw-materials, cotton-in-process, finished goods and stores and spares. The efficiency of managing these components depends upon the inventory management practices adopted. The constitution of a purchase committee and the adoption of proper techniques like ABC analysis are very essential for controlling stocks of materials. But no mill in this study had adopted the ABC analysis system in maintaining the stores record. In cotton industry the raw material is only cotton.

In all the cotton mills in Telangana, Andhra and Rayalaseema regions inventory shows an increasing trend. The major item of inventory is finished goods, and the proportion of the finished goods increased more than any other item in inventory. The turnover of inventory was low in Andhra and Rayalaseema region cotton mills. It shows the blocking of funds in finished goods and stores and spares. Among the select cotton mills Suryalatha spinning mills Ltd, Suryajyothi spinning mills Ltd and Suryavanshi spinning mills are in better position than other cotton mills.

The overall position of the percentage of inventory to total current assets in all cotton mills was high. Among the components of its inventory, the share of finished goods and stores and spares was 90 percent. It reveals that finished goods i.e. yarn constitutes major item and it was not sold in the cotton mills because of government policies and instability in selling prices.

The percentage of stores and spares to inventory decreased considerably during the study period. The Suryalatha spinning mills Ltd, Suryajyothi spinning mills Ltd and Suryavanshi spinning mills Ltd in Telangana region and Pioneer spinning and weaving mills Ltd in Rayalaseema region reduced their stocks to a great extent. In Andhra region, cotton mill i.e. Sree Akkamamba textiles Ltd has a good control over inventory in the beginning period of the study period.

Suggestions

The cotton mills should set up purchase committees for making purchase decisions and adopt appropriate inventory control system covering the fixation of lead time for the procurement of various raw materials. The system should aim at keeping the total cost of maintaining at a minimum level.
To perform the functions of inventory management such as material planning and programming inventory control, warehousing and store keeping and disposal of scrap of the mills, the mills should appoint technically qualified personnel, exclusively for this purpose.

Cotton mills those who have low inventory turnover ratio have to increase the turnover rate and decrease the investment in inventory. Telangana region cotton mills should reduce the proportion of work-in-process inventory, particularly Suryalakshmi cotton mills Ltd and Suryajyothi spinning mills Ltd. To minimize the investment on stores and spares, Suryavanshi spinning mills Ltd in Telangana region and Sree Akkamamba textiles Ltd in Andhra region should maintain a lower level of stores and spares thereby they can control other costs like carrying costs, ordering costs and stock out costs.

Cash management

Cash management is the most important function of management of business affairs. Cash management functions may be classified as custodial, flow of funds, control, obtaining bank services and investment surplus. Cash is the most liquid component of working capital. It provides liquidity to the undertaking at a cost of a part of income that could be earned through its investment. Cash management has mainly two objectives, liquidity and profitability. A proper cash management necessitates the development and application of certain practical administrative procedure to accelerate the inflow and improve the utilization of excess funds. The main objectives of keeping cash are (1) to meet the day-to-day obligations (2) to allow for contingencies (3) to take benefit from favourable market conditions and (4) to avail it of many other opportunities.

In cotton mills the requirement of cash during the first season is different from the second and third season. During the first season payments to cotton suppliers is a heavy financial burden and cash receipts through sale of yarn are not sufficient to meet the payments. Moreover in the first season quality of cotton is high and costs as well as payments are also high.
The first aspect to be observed in cash management was the percentage of cash and bank balances to the current assets. The average percentage worked out to be 2.06 percent in Suryalatha spinning mills Ltd, 3.12 percent in Suryalakshmi cotton mills Ltd, 7.72 percent in Suryajyothi spinning mills Ltd and 4.71 percent in Suryavanshi spinning mills Ltd in Telangana region. The average percentage of cash and bank balances in Rayalaseema region was low i.e. 2.90 percent when compared to Andhra region cotton mill i.e. 5.53 percent.

The analysis of the liquidity and solvency of select cotton mills revealed that the quick ratios are above the norms in all the cotton mills except Sree Akkamamba Textiles Ltd. The present study also reveals that the available cash and bank balances have not been used efficiently in most of the select cotton mills. The completion of actual liquidity attempts to measures the potentiality of the firm in meeting the current obligations on the basis of cash flows. The cash flow coverage to current liabilities ratio of the select cotton mills are 6.71 percent in Suryalatha spinning mills Ltd, 16.70 percent in Suryalakshmi cotton mills Ltd, 40.62 percent in Suryajyothi spinning mills Ltd and 7.51 percent in Suryavanshi spinning mills Ltd in Telengana region. In Pioneer spinning and weaving mills Ltd it was 39.19 percent. But in Sree Akkamamba textiles Ltd it was only 5.02 percent. The low percentages of net cash flows revealed that this mill was not in a position to meet their obligations during the study period. The efficiency of cash management is further evaluated with reference to the utilization of cash resources through sources and uses of funds. The statement of sources and uses of funds in the select cotton mills revealed that all mills used the funds for modernization and expansion programmes. The genuine working capital needs in all the mills were neglected due to redemption of current liabilities. In Andhra and Rayalaseema region cotton mills used their funds to meet the operating losses.

Suggestions

The excess of cash and bank balances of Suryajyothi spinning mills Ltd and Sree Akkamamba textiles Ltd must be reduced by redeeming the short-term loans, thereby reduce the interest burden which was very high.
The current ratio was maintained in the study period by all cotton mills except Sree Akkamamba Textiles Ltd. They have to reduce short-term loans especially wherever idle cash exists by increasing the equity share capital. All other mills have to invest their idle cash in short-term marketable securities. Otherwise, they may increase the current liabilities; thereby they can enjoy credit facilities from sundry creditors. The cash flow coverage position is to be improved in all cotton mills in Telangana, Andhra and Rayalaseema regions by retaining profits and providing depreciation and other reserves.

Profitability

Profitability is the ability of a business enterprise to make profits. The analysis of profitability involves the computation of profit ratios, based on either operating profit or net profit or on both in relation to capital employed, shareholders' investment, sales and components of operating costs. Profitability management is concerned with planning and controlling those factors which influence profits. Profit plan is a comprehensive plan covering all areas in business management. Profit planning and control involve use of certain tools of analysis like profitability ratios that enable the management to compare figures in order to derive meaningful conclusions. Profit in an undertaking is the result of the interaction of cost, selling price and volume of production and sales. Select cotton mills have shown a fluctuating trend ending with high return on capital employed when compared with the beginning. The fluctuation is due to changes in profit margin and turnover in different phases besides the input hike.

The return on capital employed was positive in all select cotton mills except Suryavanshi spinning mills Ltd that to in 2001-02 and 2002-03 in Telangana region. In case of Pioneer spinning & weaving Mills Ltd, the average of return on capital employed is 25.27 percent. But in Sree Akkamamba Textiles Ltd it is only 7.79 percent.

The profitability of the select cotton mills was further analysed through the percentage of gross profit to sales, gross operating profit to sales, earnings per share and particulars of profit /loss. Higher percentage of gross operating profit to sales implies better production management. The average gross operating profit to sales in
Suryalatha spinning mills Ltd worked out to 2.28 percent, 2.72 percent in Suryalakshmi cotton mills Ltd, 2.70 percent in Suryajyothi spinning mills Ltd and 0.76 percent in Suyavanshi spinning mills Ltd in Telangana region.

In Sree Akkamamba textiles Ltd it was 11.98 percent and the highest among the cotton mills. Gross operating profit of cotton mills depends upon the cost of production and Government policies regarding price of finished goods. The average earnings per share in Telangana region, Andhra region and Telangana region was Rs.7.06, Rs.15.32 and Rs.14.36 respectively. Comparatively Andhra region and Rayalaseema region cotton mills are better than Telangana region cotton mills.

The analysis of net operating profit to sales revealed the efficiency of the cotton mills in controlling its operating expenses i.e. selling and administrative expenses. The analysis of net operating profit to sales revealed the efficiency of the cotton mills in controlling its operating expenses i.e. selling and administrative expenses. In sample cotton mills, the Suryavanshi spinning mills Ltd incurred net operating losses to sales. The reason for it was higher operating expenses which reduced the extent of net operating profit and subsequently reduced the percentage of net operating profit to sales.

Suggestions

The mills in Telangana, Andhra and Rayalaseema regions reached well at gross profit level. The net profit is very low because the net operating profit level is poor. This deficiency can be rectified by reducing the interest burden which is an abnormal item of expenditure in the profit and loss account.

The cotton mills should adopt effective profit planning and control system. Every year, they should estimate in advance the minimum operation level through break-even analysis and fix cotton raw material on the basis of the estimated cost of production and price of yarn.

The cotton mills should adopt cost technique in order to bring down the manufacturing cost and selling and administrative costs. All the cotton mills should strengthen by developing the Finance and Cost accounting departments to collect, analyse and interpret the information on all the financial transactions and thereby identify strengths and weakness of the mills.
Cotton mills must invest considerably on research and development for the improvement of technology to realise higher rate of recovery from the cotton. The suggestions offered above for improving financial management are all viable and can be implemented without additional expenditure. These call for efficiency, competence and alertness. The cotton mills have managed to survive and do well enough in profit earnings and can better the performance if they manage their finance better.