# Chapter 6: Working Capital Management

**cash and fund flow analysis**

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6.1 Importance of cash and Fund Flow

One of the most important areas in the day-to-day management of the firms deals with the management of working capital, which is defined as all the short-term assets used in daily operations. This consists primarily of cash, marketable securities, accounts receivable and inventory. The balances in these accounts can be highly volatile as they respond very quickly to changes in the firm’s operating environment. A highly liquid firm has sufficient cash to pay its bills at all times. An illiquid firm is unable to pay its bills when due. In a financial sense, the term cash refers to all money items and sources that are immediately available to help in paying firms’ bills. On the balance sheet, cash assets include deposits in financial institutions and cash equivalent in money market funds or marketable securities. All highly liquid short-term securities are treated as cash. Most government and corporate securities are treated as cash because they may be liquidated through a telephone call. Cash is the most important current assets for the operations of the business. It is the basic input needed to keep the business running on a continuous basis. It is the money, which the firm can disburse immediately without any restriction. The term cash includes coins, currency, cheques held by the firm and balance in its bank accounts. Cash is oil that lubricates the wheel of business. Inadequate cash slows down the production and on the other hand carrying cash is expensive since it is non-earning asset. A firm that holds cash beyond its minimum requirement is lowering its potential earning. Cash is the most important current asset. It is the cash, which keeps a business going. It is the hub around which all other financial matters centre. No one can deny the fact that cash is the blood inside the business enterprise. Healthy circulation of cash in the entire business operation is the basis of business solvency. Cash is the basic input needed to keep the business running on a continuous basis; it is the ultimate output expected to be realized by selling the services or product manufactured by the firm. Ultimately every transaction in a business results either in an inflow or an outflow of cash.

Therefore, effective management of cash is the key determinant of efficient working capital management. There should be sufficient cash with a firm all the time to meet the needs of the business. Both excess and inadequate cash may degenerate a firm into a state of technical insolvency and even lead to its liquidation. It will eventually
disrupt the firm’s manufacturing operation. On the other hand excessive cash remains idle, without contributing anything towards the firm’s profitability. Moreover, holding of cash balance has an implicit cost in the form of its opportunity cost. The larger the idle cash, the greater will be its opportunity cost in the form of loss of interest which could have been earned either by investing in some interest bearing securities or by reducing the burden of interest charged by paying off the past loans. The carrying of cash and near cash reserves beyond the irreducible needs cuts assets turnover and rate of return. If the cash balance with a firm at any time is surplus or deficit, it is obvious that the finances are mismanaged. Today, when cash, like any other asset of the company, is a tool for profits, the emphasis is on right amount of cash at the right time, at the right place and at the right cost.

Meaning of Cash Management

Cash management is concerned with minimizing gun productive balances, investing temporarily cash advantageously and to making the best possible arrangement to meeting planned and unexpected demand on the firm’s cash. It involves managing of cash flows in and out of the firm, i.e. cash flows within the firm and cash balances held by the firm at a point of time. Cash management must be thought of in terms of the overall liquidity needs of the firm, specifically its current assets and liabilities. In order to reduce the influence of uncertainties with regard to cash needs and to ensure adequate liquidity, firm has to gauge the need for protective liquidity. It is necessary for business to maintain a certain amount of cash in hand or bank always, even if the other current assets are at a sustained figure. Cash is both beginning and the end of the working capital cycle – cash, inventories, receivables and cash.

Cash is the basic input needed to keep a business running on a continuous basis. It is also the ultimate output expected to be realized by selling the services or product manufactured by an enterprise.

Cash management assumes more importance than other current assets because cash is the most significant and the least productive asset that a firm holds. The aim of cash management should be to maintain adequate cash position to keep the firm’s operations in profitable manner. There are two primary reasons for a firm to hold cash:
- To meet the needs of day-to-day transactions.
- To protect the firm against uncertainties characterizing its cash flow.

Brief we can say proper cash management is required for smooth running and maximum profitability of the business. It is clear that cash is like blood stream in the human body, gives vitality and strength to a business enterprise. So it is necessary that the management of business enterprise should provide sufficient coverage to their currently maturing obligations in the form of enough cash and near cash assets, high and stable cash flows and sound profit margin. In brief while the first function of cash management increases the turnover of working capital cycle to bringing down the size of cash, the function reduces the problem of financing the working capital. Trade creditors, banks and external agencies provide finance. Cash management involves managing the monies of the firm in order to attain maximum cash availability and maximum cash income on any idle funds. Cash management is concerned with minimizing unproductive cash balances, investing temporarily excess cash advantageously, and to making the best possible arrangements for meeting planned and unexpected demand on the firm’s cash flows within the firm, and cash balances held by the firm at a point of time. Cash management must be thought of in terms of the overall liquidity needs of the firm, specifically its current assets and liabilities. In order to reduce the influence of uncertainties with regard to cash needs and to ensure adequate liquidity, firms have to gauge the need for protective liquidity. The efforts involved for this purpose usually take the form of:

Assessment of the probabilities or odds that each of these will develop within a given period in future, such as 5 years. Assessment of the probabilities and developments creating cash drains will occur at the same time. Assessment of the likely amount of cash drain that will result if each of the contingencies develops. An important policy decision regarding cash management is: what should be the optimal amount of cash balance to consider the form impact of the following factors:

1. The philosophy of the management regarding liquidity and risk of insolvency.
2. The expected cash inflows and outflows based on the cash budget forecasts encompassing long- ranging and short-range cash needs.
3.3. The size of sales in relation of fixed asset investment.

i. The degree of deviation between the expected and actual net cash flows.

ii. The maturity structure of the firm’s liabilities.

iii. The firm’s ability to borrow at short notice in the event of an emergency.

iv. Efficient planning and control of cash.

v. The status of the firm’s receivables and inventory.

vi. The credit position of the firm.

vii. The nature of business.

viii. Cash Planning

ix. Cash flows:

Inflows and outflows are inseparable parts of the business operations of all firms. The firm needs cash to invest in inventories, receivable and fixed assets and to make payments for operating expenses in order to maintain growth in sales and earnings. It is possible that a firm may be making adequate profits, but may suffer from the shortage of cash as its growing needs may be consuming cash very fast. The “Cash poor” position of the firm can be corrected if its cash needs are planned in advance. At times, a firm can have excess cash with it if its cash inflows exceed cash outflows. Such excess cash may remain idle. Again, such excess cash flows can be anticipated and properly invested, if cash planning is esorted to. Thus, cash planning can help anticipated future cash flows and needs of the firm and reduces the possibility of idle cash balances (which lowers firm’s profitability) and cash deficits (which cause firm’s failure).

Cash planning is a technique to plan for and control the use of cash. It protects the financial condition of the firm by developing a projected cash statement from a forecast of expected cash inflows and outflows for a given period. The forecasts may be based on the present operations or the anticipated future operations. Cash plans are very crucial in developing the overall operating plans of the firm. Cash planning may be done on daily, weekly or monthly basis. The period and frequency of cash planning generally depends upon the size of the firm and philosophy of management. Large firms prepare daily and weekly forecasts. Small firms may not prepare formal cash forecasts because of the non-availability of information and non-sophistication of operations. But, if, the
small firms prepare cash projections, it is done on monthly basis. As the firm grows and business operations become complex, cash planning becomes inevitable for its continuing success.

Cash forecasting and budgeting:

Cash budget is the most significant device to plan for and control the cash receipts and payments. A cash budget is a summary statement of the firm’s expected cash inflows and outs over a projected time period. It gives information on the timing, and magnitude of expected cash flows and cash balances over the projected period. This information helps the financial manager to determine the future cash needs of the firm, plan for the financing of those needs and exercise control over the cash and liquidity of the firm.

Cash forecasting-- Cash forecasts are needed to prepare cash budgets. Cash forecasting can be done on short-term or long-term basis. Generally, forecasts conferring periods of one year or less considered short-term. Those extended beyond one year are considered long-term.

Short-term forecasts:

It is comparatively easy to make short-term forecasts. The important uses of carefully developed short-term cash forecasts are:

1. It helps to determine operating cash requirements.
2. It helps to anticipate short-term financing.
3. It helps to manage money market investments.

Short-term forecasting methods-- Two most commonly used methods of short-term cash forecasting are:

1. The receipt and disbursements method.
2. The adjusted net income method.

Receipts and disbursements method:

Cash flow in and out in most of companies on a continuous basis. The prime aim of receipts and disbursements forecasts is to summarize these flows during a
predetermined period. In case of those companies where each item of income and expenses involve flow of cash, this method is favored to keep a close control over cash.

Adjusted net income method:

This method of cash forecasting involves the tracing of working capital flows. It is sometimes called the sources and uses approach. Two objectives of the adjusted net income approach are- (i) to project the company’s need for cash at some future date, and (ii) to show whether the company can generate this money internally, and if not, how much will have to either borrow or rise in the capital market.

Long-term cash forecasting:

Long-term cash forecasts are prepared to give an idea of the company’s financial requirements of distant future. They are not as detailed as the short-term forecasts are. Once a company has impact, of say, new product developments or plant acquisitions on the firm’s financial condition three, five or more years in the future.

Long-term forecasting methods- The short-term forecasting methods, the receipts and disbursements method and the adjusted net income method, can also be used in long-term cash forecasting. This method not only reflects more accurately the impact of any recent acquisitions but also foreshadows financing problems these new additions may pose for the company.

Definition of 'Fund Flow'

The net of all cash inflows and outflows in and out of various financial assets. Fund flow is usually measured on a monthly or quarterly basis. The performance of an asset or fund is not taken into account, only share redemptions (outflows) and share purchases (inflows). Net inflows create excess cash for managers to invest, which theoretically creates demand for securities such as stocks and bonds. He concept of fund is explained by different accountants and accounting bodies in different approaches. Accordingly, the word fund has different meanings as per the interpretations of different accountants and accounting bodies. These different interpretations of the concept of fund are discussed as follows:

1. Cash and bank: As per the interpretation of some accountants, Fund includes cash and bank of the enterprise only. As per this concept, the inflows and outflows of cash resources alone are considered as Flow of Fund. Accordingly, under this
concept, the Fund Flow Statement of an enterprise is prepared taking the inflows and outflows of cash resources alone.

2. Working Capital: As per this interpretation, Fund includes the Working Capital of the enterprise only. The difference between total Current Assets and total Current Liabilities of an enterprise constitutes its Working Capital (i.e., Working Capital = Current Assets – Current Liabilities). As per this concept, the inflows and outflows of the Working Capital elements alone (i.e., Current Assets and Current Liabilities) are considered as the Flow of Fund. Accordingly, under this concept, the Fund Flow Statement of an enterprise is prepared taking the inflows and outflows of Current Assets and Current Liabilities only.

**Importance of Funds Flow Statement**

Funds flow statement is an important financial tool, which analyze the changes in financial position of a firm showing the sources and applications of its funds. It provides useful information about the firm's operating, financing and investing activities during a particular period. The following points highlight the importance of funds flow statement.

1. Funds flow statement helps in identifying the change in level of current assets investment and current liabilities financing.

2. Funds flow statement helps in analyzing the changes in working capital level of a firm.

3. Funds flow statement shows the relationship of net income to the changes in funds from business operation.

4. Funds flow statement reports about past fund flow as an aid to predict future funds flow.

5. Funds flow statement helps in determining the firms' ability to pay interest and dividend, and pay debt when they become due.

6. Funds flow statement shows the firms' ability to generate long-term financing to satisfy the investment in long-term assets.

7. Funds flow statements helps in identifying the factor responsible for changes in assets, liabilities and owners' equity at two balance sheet date.

[8]
A report on the movement of funds or working capital. In a narrow sense the term fund means cash and the fund flow statement depicts the cash receipts and cash disbursements/payments. It highlights the changes in the cash receipts and payments as a cash flow statement in addition to the cash balances i.e., opening cash balance and closing cash balance. Contrary to the earlier, the fund means working capital i.e., the differences between the current assets and current liabilities.

The term flow denotes the change. Flow of funds means the change in funds or in working capital. The change on the working capital leads to the net changes taken place on the working capital i.e., especially due to either increase or decrease in the working capital. The change in the volume of the working capital due to numerous transactions. Some of the transactions may lead to increase or decrease the volume of working capital. Some other transactions neither register an increase nor decrease in the volume of working capital.

**Objectives of fund flow statement analysis:**

1. It pinpoints the mobilization of resources and the further utilization of resources
2. It highlights the financing of the general expansion of the business firms
3. It exemplifies the utilization of debt finance in the structure of financing
4. It portrays the relationship between the financing, investment, liquidity and dividend decision of the firm during the given point of time.

### 6.2 Methods of Cash and Fund Flow Analysis Cash Control Techniques:

The important techniques of controlling cash are:

i. Cash budgeting

ii. Ratio analysis

iii. Fund flow statement

iv. Financial reports

v. Linear programming

vi. Goal programming
vii. Simulation technique, and

viii. Portfolio management. Some of these are discussed below:

1. Cash budgeting—Cash budget is a time phased schedule of cash receipts and disbursements, and show the estimated cash inflows and outflows over a certain period. It is a tool of planning cash need of a business concern and serves as a cash control device. The cash budget report aims at ascertaining deviation of actual operations from budgeted ones and making it possible to compare actual with estimated cash balances at the end of each plan period. If there is a marked difference between the actual and projected balances, the cash budget for the succeeding period should be revised and included in the report.

2. Ratio analysis—It involves the use of accounting ratios rather than obsolete figures as an index of financial performance of a business concern. However, the analysis and interpretation of ratios does not only evaluate and control the over all financial performance of a concern, but also the different facts of its financial activities.

3. Fund flow statement—the analysis of financial statements through the preparation of the statements of changes in financial position of a business concern provides a very useful tool for financial planning and control. Such statements explain the charges in such or working capital and are accordingly called “Cash flow statement” or “funds flow statement”. These statements are prepared periodically to show the changes in a concern’s cash position and charges in its net working capital position, they provide evaluating techniques to the management to know the sources and uses of a concern’s fund over a period of time.

4. Financial reports—Cash reports provide a comparison of actual develops with forecast figures. They are helpful in control and revision of cash forecasts on a continual basis. Among the several types of cash reports, the important ones are—

   (i) The daily cash report,

   (ii) The daily treasury report, and

   (iii) The monthly cash report.

   The daily cash report, as the name implies, shows the cash picture on a daily basis. An amplification of the daily cash report and the daily treasury report provides a
comprehensive picture of changes in cash, marketable securities, debtors and creditors. The monthly cash report shows the picture of cash changes on a monthly basis. Required cash balance can be calculated, using historical cash turnover figures. However, the ratio shows only what is happening to the cash balance without indicating the imperfections and irregularities, caused in cash flows by the income through sales, which may be partly responsible.

(2) **Cash as Percentage of Current Assets**

The ratio of cash in current assets provides an index of current operations and, used correctly, helps determine the minimum level of cash. Monthly control of cash and his records give some indication of trends. An increasing level of cash in current assets could be caused by a reduction in the credit given by the company’s suppliers or by too high cash balance. The first may be unavoidable; the second is not. The further analysis is required to determine the cause.

Cash as Percentage to Total Assets of Selected Cement Companies has been shown in Table 6.1:

<table>
<thead>
<tr>
<th>Year</th>
<th>ACC</th>
<th>Maihar</th>
<th>Ultratech</th>
<th>Prism</th>
<th>Jaypee</th>
<th>Industry</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>1.91</td>
<td>2.42</td>
<td>2.55</td>
<td>0.54</td>
<td>2.86</td>
<td>2.06</td>
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<tr>
<td>2008-09</td>
<td>2.26</td>
<td>3.42</td>
<td>5.64</td>
<td>1.69</td>
<td>1.09</td>
<td>2.82</td>
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<tr>
<td>2009-10</td>
<td>1.76</td>
<td>3.09</td>
<td>3.13</td>
<td>2.44</td>
<td>1.02</td>
<td>2.29</td>
</tr>
<tr>
<td>2010-11</td>
<td>1.05</td>
<td>2.25</td>
<td>1.37</td>
<td>1.45</td>
<td>0.77</td>
<td>1.38</td>
</tr>
<tr>
<td>2011-12</td>
<td>0.83</td>
<td>2.63</td>
<td>0.53</td>
<td>2.39</td>
<td>0.33</td>
<td>1.34</td>
</tr>
<tr>
<td>Company Average</td>
<td>1.56</td>
<td>2.76</td>
<td>2.65</td>
<td>1.70</td>
<td>1.21</td>
<td>1.98</td>
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</table>

The Cash as percentage to Total Assets of all the cement companies shows fluctuating trend throughout the study period except India Cement which shows decreasing trend. The minimum Cash as percentage to Total Assets in ACC is 0.83 (2011-12), Maihar is 2.25 (2010-11), Ultratech is 0.53 (2009-10), Prism Cement is 0.54 (2007-2008), and in Jaypee is 0.33 (2011-12). The Maximum cash as percentage to
Total Assets in ACC is 2.26 (2008-09), Maihar is 3.42 (2008-09), Ultratech is 5.64 (2008-09), and Prism Cement is 2.44 (2009-10) and in Jaypee is 2.86 (2007-08). Cash to Net Working Capital of Selected Cement Companies has been given in table. The Cash to Net Working Capital of all the cement companies shows fluctuating trend throughout the study period except ACC and Jaypee cement which shows decreasing trend.

Cash to Current Assets of Selected Cement Companies has been presented in Table 6.2

<table>
<thead>
<tr>
<th>Year</th>
<th>ACC</th>
<th>Maihar</th>
<th>Ultratech</th>
<th>Prism</th>
<th>Jaypee</th>
<th>Industry Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>0.05</td>
<td>0.11</td>
<td>0.14</td>
<td>0.02</td>
<td>0.10</td>
<td>0.08</td>
</tr>
<tr>
<td>2008-09</td>
<td>0.07</td>
<td>0.16</td>
<td>0.30</td>
<td>0.07</td>
<td>0.03</td>
<td>0.12</td>
</tr>
<tr>
<td>2009-10</td>
<td>0.06</td>
<td>0.13</td>
<td>0.17</td>
<td>0.09</td>
<td>0.03</td>
<td>0.10</td>
</tr>
<tr>
<td>2010-11</td>
<td>0.04</td>
<td>0.10</td>
<td>0.10</td>
<td>0.06</td>
<td>0.02</td>
<td>0.06</td>
</tr>
<tr>
<td>2011-12</td>
<td>0.03</td>
<td>0.11</td>
<td>0.05</td>
<td>0.12</td>
<td>0.01</td>
<td>0.06</td>
</tr>
<tr>
<td>Company</td>
<td>0.05</td>
<td>0.12</td>
<td>0.15</td>
<td>0.07</td>
<td>0.04</td>
<td>0.09</td>
</tr>
</tbody>
</table>

Cash to Current Liabilities of Selected Cement Companies has been given in Table 6.3

<table>
<thead>
<tr>
<th>Year</th>
<th>ACC</th>
<th>Maihar</th>
<th>Ultratech</th>
<th>Prism</th>
<th>Jaypee</th>
<th>Industry Average</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007-08</td>
<td>0.07</td>
<td>0.33</td>
<td>0.45</td>
<td>0.06</td>
<td>0.22</td>
<td>0.22</td>
</tr>
<tr>
<td>2008-09</td>
<td>0.14</td>
<td>0.38</td>
<td>1.12</td>
<td>0.16</td>
<td>0.11</td>
<td>0.38</td>
</tr>
<tr>
<td>2009-10</td>
<td>0.10</td>
<td>0.31</td>
<td>0.41</td>
<td>0.23</td>
<td>0.08</td>
<td>0.23</td>
</tr>
<tr>
<td>2010-11</td>
<td>0.06</td>
<td>0.15</td>
<td>0.21</td>
<td>0.19</td>
<td>0.07</td>
<td>0.13</td>
</tr>
<tr>
<td>2011-12</td>
<td>0.05</td>
<td>0.09</td>
<td>0.06</td>
<td>0.32</td>
<td>0.03</td>
<td>0.11</td>
</tr>
<tr>
<td>Company</td>
<td>0.08</td>
<td>0.25</td>
<td>0.45</td>
<td>0.19</td>
<td>0.10</td>
<td>0.22</td>
</tr>
</tbody>
</table>

Methods of preparing Fund Flow Statement

Step in the preparation of fund flow Statement

a. First and foremost method is to prepare the statement of changes in working capital
   i.e. identify the flow of fund/movement of fund through the detection of changes in
   the volume working capital.
b. Second step is the preparation of Non-Current A/C items-changes in the volume of noncore A/C have to be prepared only in order to quantify the flow fund i-e either sources or applicant of fund. The third step is the preparation adjusted profit & Loss A/C.

1. **Schedule of Changes in Working Capital**

   The Ultimate purpose of preparation the schedule of changes in the working capital is to be change in the volume of net working capital which envisages either sources or application of fund. The schedule of changes is focused as follows:

   The first method is widely used method by all in determining the volume of fund from operations (FFS) under the Net Profit Method, fund flow from operations can be computed.

2. **Net Profit Method**

   Under this method, fund from operations can be determined in two different

   The first method is through the statement format Net Profit from the Profit from the Profit & Loss A/C

   **A. Non Funding Expenses**

   Loss on Sale of Fixed Assets

   Loss on Sale of Long Term Investment

   Loss on Redemption Debentures / Preference Shares

   **B. Non Operating Expenses**

   Depreciation of Fixed Assets

   **C. Intangible Assets**

   Amortization of Goodwill

   Amortization of Patent

   Amortization of Trade Mark
D. **Fictitious Assets**

Writing off Preliminary expense

E. **Profit Appropriation**

Transfer to General Reserve

F. **Non funding Profits**

Profit on Sale of Fixed Assets
Profit on Sale of Long Term Investment
Profit on Redemption Debentures / Preference Shares

G. **No Operating Incomes**

Dividend Received
Interest Received
Rent Received

Fund from Operation / Fund Lost in Operation

Second Method of determining the fund from operation under the first classification, is the Accounting Statement Format.

3. **Sales Method**

Under this method, the following is the statement format is used to arrive fund flow from operation

**Sources**

Sales
Stock at the end

**Application**

Stock at Opening

[14]
Net Purchase (Purchase – Return)

Wages

Salaries

Telephone Expenses

Electricity Charges

Office Stationary Expenses

Other Operating Each Expense

6.3 Evaluation of Cash and Fund Flow Analysis

Proper cash management is “life blood of a business” all the more so in product like cement where the value of sales of all major cement producers is in few hundred Crore of rupees each. It has been analyzed in this chapter what should be an ideal cash-sales ratio and what actually it is for cement industry in general and for various regions and Dalmia Cement in particular and what are the factors responsible for current state of affairs. Cash is needed to meet day-to-day transactions for purchase of raw materials; payment of wages, salaries and royalty and factory overheads; payment for coal, electricity, furnaces oil and other inputs and goods in process; cash is also blocked in finished goods stock at factory and depots and distribution channels, advance payment of taxes and other future liabilities and sales on credit. On the one side purchase on credit, advance receipts for supplies and other short-term receipts are other side of the coin. All these factors affect not only overall current assets but also cash management. It is, therefore, necessary to properly understand and plan current assets cycle, which may be summarized as under for cement industry.

The cash is required basically to meet day-to-day running of business for purchase of materials, other inputs, and energy payment of wages, salaries, overheads, and consumables. Funds are also required to meet cost of inventories (raw- materials, spares, consumables, goods in process, finished products and providing credit to buyers). Sometime funds are also needed to pay advance of excise duty, sales tax, property and water tax and income tax.

Many a times emergencies also arise which are not foreseen and reserve cash has
to be kept to meet uncertainties with regard to cash receipts and payment whether for current assets and liabilities or to meet long-term funds. The proper cash management is given great importance in financial management with a view to minimize its cost, ensure adequate cash for all requirements and avoid surplus cash with the organization. The aim of cash management is to minimize cost of interest on borrowings, earning maximum interest from surplus funds and avoid or at least reduce uncertainties of surplus or short funds so that need of borrowings to meet emergencies is avoided. At the same time planning is needed for proper investment of surplus funds whether in securities, additional inventories or utilizes them for prepaid payment of borrowings. In order to ensure above objectives it is necessary to take a number of steps for cash planning such as cash deciding policy for credit purchase and sales. It also implies to fix optimum level of inventories and investment of surplus funds. To what extent these planning tools have been adopted by cement industry in last one decade has been studied with the help of published data of selected cement companies and discussions with the industry.

Money, as is well assumed, has a time value. Inflationary economy (which is the case in India) current value of money is more than future value but if one takes the gain in the value of stocks the above statement is not always true. If the prices of inputs and outputs rise faster than rate of interest it will be more profitable to minimize cash balances. But as in India the rate of interest on working capital loans from banks is between 18-20 per cent and the rate of inflation is less, it is advisable to manage with the minimum possible cash but it is not always in the hands of management because of changing market and economic conditions and policies of the government. In our country cement industry has been victim of uncertainties. There is no fixed trend in the rate of growth in demand of cement. There have been periods of surpluses and shortages as described in earlier chapter soon after decontrol on production and prices number of new cement plants were established all over the country creating situation of surplus and increased competition forcing industry to give liberal credit to trade and creating situation of surplus and increased competition forcing industry to give liberal credit to trade and industry requiring more cash resources. Then there was a period of tight supplies and now again sales are less than capacity forcing industry to reduce prices and provide more liberal credit to buyers.

In case of cement supplies to the PWD and other government departments and
consumers (which accounts generally to more than one-third of sales). Credit has to be given and the terms by convention are decided by buyers and not by seller. Thus producers to a great extent are not able to manage cash as they wish and are governed by market forces.

The cement though is not seasonal industry consumption goes down during rainy season because construction becomes difficult and some areas become unapproachable in July-September. In these areas sales are accelerated in April-July to keep stock for rainy season. But it is a fact that market is sluggish in monsoon season not only because of dampening in construction activity but also due to risk of spoilage of cement in transit during rainy season which reduces its movement. To what extent this factor has actually affected cash flow and cash management could not be studied in next part of analysis because only financial year-end data could become available. In the absence of monthly cash flow it has not been possible to study impact of this factor on cash sales ratio.

The traditional concept of profit and loss account and balance sheet has a limited role to play in financial analysis. The profit and loss account reflects the results of the business operations for a specified period of time. It takes into account only the expenses incurred and income received during the accounting period. The balance sheet gives a summary of the assets and liabilities at a particular period of time. And at the same time, balance sheet does not explain the details about the movement of funds. In actual practice, a business concern receives funds from various sources and invested in various ways of investment. It is a continuous process. The ultimate aim of the financial management is to study and control these funds in order to maintain the solvency and financial soundness of the firm. For the purpose of complete study of sources and applications of funds over the accounting period, a separate statement is essential to find the periodical increase or decrease of such funds f an enterprise. This statement is called fund flow statement. Fund flow statement is an invaluable analytical tool for a financial manager for the purpose of evaluating the employment of funds by a firm and also to assess sources of such funds. Following are the important managerial uses of fund flow statement.

1. The foremost use of the fund flow statement is to explain the reasons for changes in the assets and liabilities between two balance sheet dates.
2. Fund flow statement gives details about the funds obtained and used in past. Based upon this detail; manager can take correct actions at appropriate times.

3. Fund flow statement acts as a control device when compared with budgeted figures. It also gives guidance to the finance manager for taking remedial action if there is any deviation.

4. It helps the management to formulate various financial policies-viz dividend, bonus etc.

5. It gives guidance to the management with regard to working capital. Through fund flow statement, management can take proper steps for effective utilization of surplus working capital or in case of inadequacy; suitable arrangement can be made for improving the working capital position.

6. It identifies the strong and weak financial areas of the firm.

7. It gives the answers for various financial intricate questions:
   a. How much funds were generated?
   b. How were the funds used?

8. Effective utilization of available resources and scarce resources should be allocated according to the preferential needs.

9. With the help of the fund flow statement, financial and lending institutions can easily evaluate the credit worthiness and repaying capacity of the borrowing company.

10. It enables the management to reformulate the firm’s financial activity on the basis of the statement.
References


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