CHAPTER – 6
MANAGEMENT OF RECEIVABLE AND CASH

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CHAPTER - 6

MANAGEMENT OF RECEIVABLE AND CASH

MEANING OF RECEIVABLES

The term receivable is defined as “debt owed to the firm by customers arising from sale of goods or services in the ordinary course of business.” When a firm makes an ordinary sale of goods or services and does not receive payment, the firm grants trade credit and creates accounts receivable which would be collected in the future. According to Robert N. Anthony, “Accounts receivables are the amounts owned to the business enterprise, usually by its customers. Sometimes this item is broken down into trade account receivable and other accounts receivable, the former refers to the amount owned by customers, and the latter refers to the amount owed by employees and others.”

MANAGEMENT OF RECEIVABLES

Meaning and Objective

Receivables Management is also called trade credit management. Accounts Receivables represent as extension of credit to customers, allowing them a reasonable period of time in which to pay for the goods which they have received.
One of the major responsibilities of finance area now-a-days is to assist the top management in the task of formulating a suitable credit policy. This involves management of receivables which represent a sizable portion of circulating funds. In cash sales inflow of cash is almost immediate; but in credit sales, there is a time-lag between sale of goods and the inflow of cash. In large business dealings, cash sales are rare and selling on credit has become the order of the day. With growth in credit sales, considerable part of the working fund is tied up in receivables. The size and duration of funds invested in receivables depend, by and large, on credit terms, credit standards and the collection policy of the firm.

The objective of receivable management is achieving a balance which result in the combination of sales and profit rates which maximises the overall return on the investment of the firm.

The two basic liquidity goals in receivables management concentrate on (1) prospects of collecting receivables when they become due; and (2) prospect of shortening future receivables maturities. In other words, liquidity increases as the certainty of collecting the receivables at maturity increases and vice-versa.
The basic goal of credit management is to maximise the value of the firm by achieving a trade off between liquidity and profitability. The purpose of credit management is not to maximise sales, nor to minimise the risk of bad debt. If the objective is to maximise sales, then the firm would sell on credit to all. On the contrary, if minimisation of bad debt risk were the aim, then the firm would not sell on credit to anyone. In fact, the firm should manage its credit in such a way that sales are expanded to an extent to which risk remains within an acceptable limit. Thus, to achieve the goal of maximising the value, the firm should manage its trade credit effectively. The main purpose should be:

1. to obtain optimum (not maximum) value of sales;
2. to control the cost of credit and keep it at minimum; and
3. to maintain investment in trade debtors at optimum level.

The purpose of credit management is not sales maximisation, but efficient and effective credit management. It does help to expand sales and can prove to be an effective tool of marketing. Well administered credit means profitable credit accounts. Granting of credit and its management involves costs. To maximise the value of the firm. These costs must be controlled and
they should remain within acceptable limits. These costs include: (i) the credit administration expenses; (ii) bad debt losses, (iii) and opportunity costs of the funds tied up in receivables. The aim of credit management should be to regulate and control these costs as they cannot be eliminated altogether. These costs can be reduced to zero, if no credit is granted. But the profits foregone on the expected volume of sales arising due to the extension of credit may be much more than the costs eliminated. Therefore, the objective should be to keep the costs to the minimum.

**OPTIMUM CREDIT POLICY**

Credit facility is normally allowed by every firm to their customers; although the terms and the extent of trade credit allowed may vary according to local tradition and conditions. Degree of competition credit norms prevailing in industry and general economic environmental conditions are some of the important external factors within which a business firm has to devise its credit policy. A credit policy should be dynamic and flexible one so that it may suit the changed conditions.
Credit Policy of a concern is influenced by many factors, such as the types of products sold, types of customers, profit margin, general economic conditions etc.

Credit Policy is very important part of the overall strategy of a concern. While formulating a credit policy, every firm has to take into consideration the following points: (i) Credit terms, (ii) Credit Standard, (iii) Collections policy.

(i) CREDIT TERMS

The two factors which emerge in this context are:

a) the credit period; and

b) the cash discount allowed to customers for making easy payment (before the due date).

Credit period is the time duration for which credit is to be allowed. In this respect, firms usually follow the norms being pursued or are prevailing in the industry. Credit period is generally stated in terms of a net date.

Cash discount is another aspect of credit terms. Many firms’ offer cash discount to their customers in order to induce them to pay their bills early. The cash discount terms indicate the rate of
discount and the period for which discount has to be offered. If a customer does not avail this offer, he is expected to make the payment by the net date. In fact, the credit terms indicate (a) the rate of cash discount; (b) the discount period; and (c) the credit period.

Credit terms can be used as an instrument to push sales. The most desirable credit terms, which increase the overall profitability of the firm, should be offered to customers.

CREDIT STANDARD

The credit standard followed by the firm has an impact on sales and receivables. The sales and receivables levels are likely to be high if the credit standards of the firm are relatively loose. In contrast, if the firm has relatively tight credit standards, the sales and receivables levels are expected to be relatively low. The firm’s credit standard are influenced by “three C’s” of credit: (a) character – the willingness of the customer to pay; (b) capacity – the ability of the customer to pay; and (c) conditions – the prevailing economic conditions.
Normally, a firm should lower its credit standards to the extent profitability of increased sales exceeds the associated costs. The costs arising due to credit standard relaxation are administrative costs of supervising additional accounts and servicing increased volume of receivables, bad debt losses, production and selling costs and the cost resulting from a slower average collection period. When the credit standards are relaxed, the collection period will be lengthened in case of the new customers. This may tempt the existing customers not to pay bills in time.

The extent to which credit standards can be liberalised should depend upon the matching between the profits arising due to increased sales and the costs to be incurred on the increased sales.

iii) COLLECTION POLICY

A collection policy is needed because all customers do not pay the firm’s bills in time. Some customers are slow-payers while some are non-payers. The collection policy should, therefore, aim at accelerating collections from slow-payers and reducing bad debt losses.
The main objectives of a good collection policy should be two-fold. Firstly, it should succeed in collecting overdue accounts, so as to minimise bad debts. Secondly it should aim at restricting or tightening of credit to slow-paying customers.

PERFORMANCE EVALUATION OF RECEIVABLES MANAGEMENT

The performance of receivables management in the selected textile companies in Uttar Pradesh has been evaluated by analysing the size and composition of receivables. They have been discussed below:

(A) Size of Receivables

The size of receivables is closely associated with firm’s trade terms, which contains the period of credit, the rate of discount and collection policies etc. But the most important factor is determining the size of receivables in the level of a firm’s credit sales.

Receivables include sundry debtors and loan and advances. The size of receivable in the selected textile mills can be seen in table 6(A).
Table – 6(A)
SIZE OF RECEIVABLES IN THE SELECTED TEXTILE MANUFACTURING COMPANIES IN U.P. FROM 1998-99 TO 2003-2004

<table>
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<tbody>
<tr>
<td>The British India Corporation Ltd.</td>
<td>4,13,57,352 (100)</td>
<td>3,31,76,360 (80.21)</td>
<td>5,60,84,971 (135.61)</td>
<td>6,04,47,789 (146.15)</td>
<td>10,67,88,434 (258.20)</td>
<td>14,22,55,888 (343.96)</td>
</tr>
<tr>
<td>The Elgin Mills Company Limited</td>
<td>1,58,49,270 (100)</td>
<td>1,81,11,546 (114.27)</td>
<td>1,36,39,615 (86.05)</td>
<td>2,53,03,492 (159.65)</td>
<td>7,25,90,423 (458.00)</td>
<td>N.A.</td>
</tr>
<tr>
<td>Cawnpore Textiles Ltd.</td>
<td>1,94,63,136 (100)</td>
<td>2,13,11,603 (109.49)</td>
<td>1,98,54,866 (102.01)</td>
<td>65,14,960 (33.47)</td>
<td>1,53,12,393 (78.67)</td>
<td>N.A.</td>
</tr>
</tbody>
</table>

Source: - Annual Reports & Accounts of the Company under study.
It is evident from the above table that there was an increasing trend in the size of receivables of the British India Corporation Ltd. during the study period except in the year 1999-2000 which was 80.21 per cent as compared to 100 per cent in 1998-99 taken as the base year.

In case of the Elgin Mills Company Ltd. in the year 1999-2000 the size of receivables showed an increasing trend which was 114.27 per cent as compared to 100 per cent in 1998-99 taken as the base year. It showed decreasing trend in 2000-2001 and again increased in the remaining years.

Table 6(A) shows that Cawnpore Textiles Ltd. showed an increasing trend in the year 1999-2000 as compared to 100 per cent in 1998-99 taken as base year. It showed decreasing trend in its receivables from 2000-2001 to 2002-2003. It was 102.01 per cent in 2000-2001 and 33.47 per cent and 78.67 per cent in 2001-2002 and 2002-2003 respectively.

The above analysis reveals that all the textile companies under study showed a decreasing as well as increasing trend.
GROWTH OF TOTAL SALES AND TOTAL RECEIVABLES

To have faster growth in receivables, liberal credit terms should be offered so that existing customers purchase more and new customers can be created. Disproportion in growth of receivables results in loss than profit incremental sales due to the inclusion of lower quality of debtors. The following table shows the behaviour of sales and receivables of the selected textile manufacturing companies in U.P. during the period under study.

Table 6(B)
PROGRESSIVE BASE YEAR PERCENTAGE GROWTH OF TOTAL RECEIVABLES AND TOTAL SALES OF THE SELECTED TEXTILE MANUFACTURING COMPANIES IN U.P. TAKEN TOGETHER FROM 1998-99 TO 2003-2004

<table>
<thead>
<tr>
<th>Year</th>
<th>Total Receivables</th>
<th>Growth of Total Receivables</th>
<th>Total Sales</th>
<th>Growth of total Sales</th>
</tr>
</thead>
<tbody>
<tr>
<td>1998-1999</td>
<td>76669758</td>
<td>-</td>
<td>69169418</td>
<td>-</td>
</tr>
<tr>
<td>1999-2000</td>
<td>72599509</td>
<td>5.30</td>
<td>110998146</td>
<td>60.47</td>
</tr>
<tr>
<td>2000-2001</td>
<td>89579452</td>
<td>23.38</td>
<td>114816287</td>
<td>3.43</td>
</tr>
<tr>
<td>2001-2002</td>
<td>92266241</td>
<td>2.99</td>
<td>152558142</td>
<td>32.87</td>
</tr>
<tr>
<td>2002-2003</td>
<td>194691250</td>
<td>111.01</td>
<td>140017394</td>
<td>- 8.22</td>
</tr>
<tr>
<td>2003-2004</td>
<td>142255888</td>
<td>- 26.93</td>
<td>147400103</td>
<td>5.27</td>
</tr>
</tbody>
</table>
The above table reveals that the growth rate in receivables was lower than the sales in 99-2000. The sales were 60.47 per cent in 99-2000 whereas -5.30 per cent in receivables. The rate of growth in receivable was more in 2000-2001 but the sales decreased. In 2001-2002 the sales increased with 32.87 per cent but the receivables rate decreased which was 2.99 per cent. In 2002-2003 the rate of growth of receivables was 111.01 per cent compared to sale growth which was at the declining rate -8.22. In 2003-04 sales showed increase in growth rate and was 5.27 per cent, here receivables decreased its growth and was -26.93.

(B) COMPOSITION OF RECEIVABLES

Receivables comprise the total of sundry debtors and loans and advances. The study of the composition of receivables helps to locate where receivables concentrated the most.

(a) Sundry Debtors – The table 5(c) shows the size of sundry debtors in the selected textile manufacturing companies in U.P.

In case of the British India Corporation Ltd. there was an increasing trend in first two years of study, which was 33.59 and 56.40 per cent in the year 1999-2000 and 2000-2001 respectively.
The size of sundry debtors decreased to 38.87 per cent in 2002-2002 followed by another decrease in the year 2002-2003, which was 18.87 per cent. It showed an increase in the last year of study which was 22.91 per cent. According to the table 6(c). The Elgin Mills Company Ltd. showed a fluctuating trend in the size of sundry debtors. In 1998-99 the percentage was 59.27, followed by a decrease in 1999-2000 which was 50.94 per cent. In 2000-2001 it again showed an increasing trend by showing a rise to 60.36 per cent in 2000-2001. It again showed a decrease in the years 2001-2002 and 2002-2003 which was 24.52 per cent and 8.36 per cent respectively.

It is evident from the table 6(C) that there was fluctuating trend in the size of sundry debtors of Cawnpore Textiles Ltd. during the study period. It was the highest in 1998-99, i.e. Rs.77,00,276 and the lowest in 2002-2003, i.e. Rs.26,45,140. The percentage of sundry debtors was 39.56 per cent in 1998-99 followed by a decrease in the year 1999-2000 and 2000-2001. It increased in 2001-2002 following by a decrease in 2002-2003.

On the basis of the analysis, we may conclude that all the companies under study showed a fluctuating trend. The average of
**Table – 6(C)**


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<tbody>
<tr>
<td>The British India Corporation Ltd.</td>
<td>1,19,36,661 (28.86)</td>
<td>1,11,46,426 (33.59)</td>
<td>3,16,37,152 (56.40)</td>
<td>2,34,99,282 (38.87)</td>
<td>2,01,51,714 (18.87)</td>
<td>3,26,02,032 (22.91)</td>
<td>(33.25)</td>
</tr>
<tr>
<td>The Elgin Mills Company Limited</td>
<td>93,94,552 (59.27)</td>
<td>92,27,074 (50.94)</td>
<td>82,33,315 (60.36)</td>
<td>62,05,861 (24.52)</td>
<td>60,69,717 (8.36)</td>
<td>N.A.</td>
<td>(40.69)</td>
</tr>
<tr>
<td>Cawnpore Textiles Ltd.</td>
<td>77,00,276 (39.56)</td>
<td>75,34,576 (35.35)</td>
<td>52,50,074 (26.440</td>
<td>26,44,570 (40.59)</td>
<td>26,45,140 (17.27)</td>
<td>N.A.</td>
<td>(31.84)</td>
</tr>
</tbody>
</table>

Source:- Annual Reports & Accounts of the Company under study.
the percentage of sundry debtors to receivable in case of the Elgin Mills Company Ltd. was the highest which was 40.69 per cent. Next was the British India Corporation Ltd. (33.25 per cent). The lowest was Cawnpore Textiles Ltd. (31.84 per cent).

(b) **Loans & Advances**

Table 6(D) explains the size of loans and advances in the selected textile companies in Uttar Pradesh under study.

In case of the British India Corporation Ltd. the size of loans and advances showed a decreasing trend in 1999-2000 and 2000-2001 which was 66.40 and 43.59 per cent respectively. It increased in 2001-2002 (61.12 per cent) and 2002-2003 (81.12 per cent). It decreased in 2003-2004 which came to 77.08 per cent.

It is clear from table 6(D) that the size of loans and advances of the Elgin Mills Company Ltd. registered a rising trend during the period of study except in the year 2000-2001 which was 39.63 per cent. The percentage of loans and advances to receivables varied between 39.63 per cent and 91.63 per cent.

There was a fluctuating trend in the size of loans and advances of Cawnpore Textiles Ltd. It was maximum
### Table 6(D)


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</tr>
</thead>
<tbody>
<tr>
<td>The British India Corporation Ltd.</td>
<td>2,94,20,691 (71.13)</td>
<td>2,20,29,934 (66.40)</td>
<td>2,44,47,819 (43.59)</td>
<td>3,69,48,507 (61.12)</td>
<td>8,66,36,720 (81.12)</td>
<td>10,96,53,856 (77.08)</td>
<td>(66.74)</td>
</tr>
<tr>
<td>The Elgin Mills Company Limited</td>
<td>64,54,718 (40.72)</td>
<td>88,84,472 (49.05)</td>
<td>54,06,300 (39.63)</td>
<td>1,90,97,631 (75.47)</td>
<td>6,65,20,706 (91.63)</td>
<td>N.A.</td>
<td>(59.3)</td>
</tr>
<tr>
<td>Cawnpore Textiles Ltd.</td>
<td>1,17,62,860 (60.43)</td>
<td>1,37,77,027 (64.64)</td>
<td>1,46,04,792 (73.55)</td>
<td>38,70,390 (59.40)</td>
<td>1,26,67,253 (82.72)</td>
<td>N.A.</td>
<td>(68.14)</td>
</tr>
</tbody>
</table>

Source: Annual Reports & Accounts of the Company under study.

On the basis of the average percentage of loans and advances to receivables of the Companies under study, it may be said that the Cawnpore Textiles Ltd. had the highest percentage which was 68.14 percent. The British India Corporation Ltd. (66.74 percent) and The Elgin Mills Company Ltd. (59.3 per cent).

CASH MANAGEMENT

The role of cash and other liquid assets in business should never be under-estimated. Cash is the most liquid of all other assets. The operating cycle starts with a cash-outflow and ends with a cash-inflow. In order to start and complete a chain of operating cycles, one after other, adequate level of cash must be maintained in business through-out the operating period.

Cash includes coins, currency notes, cheques, cash balance at bank.
Cash is the basic input needed to keep the business running on a continuous basis. It is also the ultimate output expected to be realised by selling the service or product manufactured by the firm. The firm should keep sufficient neither more nor less. Cash shortage will disrupt the firm’s manufacturing operation, while excessive cash will simply remain idle, without contributing anything towards the firm’s profitability.

Cash is the money which the firm can disburse immediately without any restriction. Other than coins, currency and cheques, near cash items, such as marketable securities or bank time-deposits are also included in cash.

MEANING OF CASH MANAGEMENT

Cash management is concerned with the managing of (i) cash flows into and out of the firm, (ii) cash flows within the firm and (iii) cash balances held by the firm at a point of time. 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 is to maintain adequate cash position to keep the firm sufficiently liquid and to use excess cash in some profitable way.

Cash management is one of the key areas of working capital management. Apart from the fact that it is the most liquid current asset, cash is the common denominator to which all current assets can be reduced because the other major liquid assets, i.e., receivables and inventory get eventually converted into cash. This underlines the significance of cash management.

The management of cash is important because it is difficult to predict cash flows accurately and that there is no perfect coincidence between the inflows and outflows of cash.

Cash management is also important because cash constitutes the smallest portion of the total current assets, yet management's considerable time has to be devoted in managing it.

**STRATEGIES FOR CASH MANAGEMENT**

The firm should evolve strategies regarding the following four facets of cash management:
1. **Cash planning** – Cash inflows and outflows should be planned to project cash surplus or deficit for each period of the planning period. Cash budget should be prepared for this purpose.

2. **Managing the Cash flows** – The flow of cash – inflow and outflow should be properly managed. The inflows of cash should be accelerated while, as far as possible, the outflows of cash should be decelerated.

3. **Optimum Cash level** – The firm should decide about the appropriate level of cash balances. The cost of excess cash and danger of cash deficiency should be matched to determine the optimum level of cash balances.

4. **Investing idle cash** – The idle cash or precautionary cash balances should be properly invested to earn profits. The firm should decide about the division of such cash balances between bank deposits and marketable securities.

**MOTIVES FOR HOLDING CASH**

The firm’s need to hold cash may be attributed to the following three motives:-
i) The transaction motive.

ii) The precautionary motive.

iii) The speculative motive.

i) The Transaction Motive – The transaction motive requires a firm to hold cash to conduct its business in the ordinary course. The firm needs cash primarily to make payments for purchases, wages, operating expenses, taxes, dividends etc. The need to hold cash would not arise; if there were perfect synchronisation between cash receipts and cash payments, i.e. enough cash is received when the payment has to be made. But cash receipts and payments are not perfectly synchronised. Sometimes cash receipts exceed cash payments, while at other times cash payments are more than cash receipts. For those periods, when cash payments exceed cash receipts, the firm should maintain some cash balance to be able to make the required payments. For transactions purposes, a firm may invest its cash in marketable securities. Usually the firm will purchase the securities whose maturity corresponds with some anticipated payments, such as dividends, taxes etc. in future.

ii) The precautionary Motive – The precautionary motive is the need to hold cash to meet any contingencies in future. It provides a
cushion or buffer to withstand some unexpected emergency. The precautionary amount of cash depends upon the predictability of cash flows. If cash flows can be predicted with accuracy, less cash will be maintained against an emergency. The amount of precautionary cash is also influenced by the firm’s ability to borrow at short notice, when the need arises. Stronger the ability of the firm to borrow at short notice less the need for precautionary balance. The precautionary balance may be kept in cash and marketable securities. Marketable securities play an important role here. The amount of cash set aside for precautionary reasons is not expected to earn anything; therefore, the firm should attempt to earn some profit on it. Such funds should be invested in high liquid and low-risk marketable securities. Precautionary balances should thus be held more in marketable securities and relatively less in cash.

iii) The Speculative Motive – The speculative motive relates to the holding of cash for investing in profit making opportunities as and when they arise. The opportunity to make profit may arise when the security price changes. The firm will hold cash, when it is expected that interest rates will rise and security prices will fall.
Securities can be purchased when the interest rate is expected to fall; the firm will benefit by the subsequent fall in interest rates and increase in security prices.

The firm may also speculate on materials’ prices. If it is expected that materials price will fall the firm can postpone materials purchasing and make purchases in future when price actually falls. Some firms may hold cash for speculative purposes. By and large, business firms do not engage in speculations. Thus, the primary motives to hold cash and marketable securities are the transactions motive and the precautionary motive. The firm must decide the quantum of transactions and precautionary balances to be held. This depends upon the following factors:-

1. The expected cash inflows and outflows based on the cash budget and forecast, encompassing long and short-range cash needs of the firm.

2. The decree of deviation between the expected and actual net cash flows.

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

4. The firm’s ability to borrow at short notice, in the event of any emergency.
5. The philosophy of management regarding liquidity and risk of insolvency.

6. The efficient planning and control of cash.

OBJECTIVES

The basic objectives of cash management are two fold:

(a) to meet the disbursement needs (payment schedule)

(b) to minimise funds committed to cash balances

1) Meeting the Payments Schedule

In the normal course of business, firms have to make payments of cash on a continuous and regular basis to suppliers of goods, employees and so on. At the same time, there is a constant inflow of cash through collection from debtors. Cash is, therefore, aptly described as the "oil to lubricate the ever turning wheels of business: without it the process grinds to a stop." A basic objective of cash management is to meet the payment schedule, i.e. to have sufficient cash to meet the cash disbursement needs of a firm. The importance of sufficient cash to meet the payment schedule can hardly be over emphasized. The advantages of adequate cash are:-
i) it prevents insolvency or bankruptcy arising out of the inability of a firm to meet its obligations;

ii) the relationship with the bank is not strained.

iii) it helps in fostering good relations with trader creditors and suppliers of raw materials, as prompt payment may help their own cash management.

iv) a trade discount can be availed of if payment is made within the due date.

2) Minimising Funds committed to Cash Balance

The second objective of cash management is to minimise cash balances. In minimising the cash balances two conflicting aspects have to be reconciled. A high level of cash balances will ensure prompt payment together with all the advantages. But it also implies that large funds will remain idle, as cash is a non-earning asset and the firm will have to forego profits. A low level of cash balances, on the other hand, may mean failure to meet the payment schedule. The aim of cash management should be to have an optimal amount of cash balances.
CASH MANAGEMENT 'TEHCNIQUES / PROCESS'

In managing cash efficiently, the cash inflow process can be accelerated through systematic planning and refined techniques.

Once the customer makes the payment by writing a cheque in favour of the firm, the collection can be expedited by prompt encashment of the cheque. It will be recalled that there is a lag between the time a cheque is prepared and mailed by the customer and the time the funds are included in the cash reservoir of the firm. Within this time interval three steps are involved:

(a) transit or mailing time, i.e., the time taken by the post offices to transfer the cheque from the customers to the firm. This delay or lag is referred to as postal float.

(b) time taken in processing the cheque within the firm before they are deposited in the banks, termed as lethargy; and

(c) Collection time within the bank, i.e. the time taken by the bank in collecting the payment from the customer's bank. This is called bank float.

The early conversion of payment into cash, as a technique to speed-up collection of accounts receivable, is done to reduce the
time lag between posting of the cheque by the customer and the realisation of money by the firm.

The postal float, lethargy and bank float are collectively referred to as deposit float. The term deposit float is defined as the sum of cheques written by customers that are not yet usable by the firm. The collection of accounts receivable can be considerably accelerated, by reducing transit, processing and collection time. An important cash management technique is reduction in deposit float. This is possible if a firm adopts a policy of decentralised collections. The principle methods of establishing a decentralised collection network are:

(a) Concentration Bank, and
(b) Lock box system.

CONCENTRATION BANKING

In this system of decentralised collection of accounts receivable, large firms which have large number of branches at different places, select some of these which are strategically located as collection centres for receiving payment from customers. Instead of all the payments being collected at the head office of the firm, the cheques for a certain geographical area are collected at a
specified local collection centre. Under this arrangement, the customers are required to send their payments (cheques) to the collection centre covering the area in which they live and these are deposited in the local account of the concerned collection centre, after meeting local expenses, if any. Funds beyond a predetermined minimum are transferred daily to a central or disbursing or concentration bank or account. A concentration bank is one with which the firm has a major account—usually a disbursement account. Hence this arrangement is referred to as concentration banking. Concentration banking, as a system of decentralised billing and multiple collection points, is a useful technique to expedite the collection of accounts receivable. It reduces the time needed in the collection process by reducing the mailing time. Since the collection centres are near the customers, the time involved in sending the bill to the customer is reduced. Moreover, the time-lag between the despatch of the cheque by the customer and its receipt by the firm is also reduced. Mailing time is saved both in respect of sending the bill to the customers as well as in the receipt of payment. The second reason as to why deposit float is reduced by concentration banking is that the banks of the firm as well as the customers may be in close proximity. Thus,
the arrangement of multiple collection centres with concentration banking results in a saving of time in both mailing and clearance of customer payments and leads to a reduction in the operating cash requirements. Another advantage is that concentration permits the firm to 'store' its cash more efficiently. This is so mainly because by pooling funds for disbursement in the single account, the aggregate requirement for cash balances is lower than it would be if balances were maintained at cash branch office.

(2) LOCK-BOX SYSTEM

The concentration banking arrangement is instrumental in reducing the time involved in mailing and collection. But with this system of collection of accounts receivable, processing for purposes of internal accounting is involved, i.e. sometime elapses before a cheque is deposited by the local collection centre in its account. The lock box system takes care of this kind of problem, apart from effecting economy in mailing and clearance times. Under this arrangement, firms hire a post office box at important collection centres. The customers are required to remit payments to the lock-box. The local banks of the firm, at the respective places, are from the customers. usually the authorised banks pick
up the cheques several times a day and deposit them in the firm's accounts. After crediting the account of the firm, the banks send a deposit slip along with the list of payments and other enclosures, if any, to the firm by way of proof and record of the collection.

Thus, the lock-box system is like concentration banking in that the collection is decentralised and is done at branch level. But they differ in one very important respect. While the customer sends the cheques under the concentration banking arrangement to the collection centres, it sends them to a post office box under the lock-box system. The cheques are directly received by the bank which empties the box and not from the firm or its local branch.

In a way, the lock-box arrangement is an improvement over the concentration banking system. Its superiority arises from the fact that one step in the collection process is eliminated with the use of lock-box: the receipt and deposit of cheques by the firm. In other words, the processing time within the firm before depositing a cheque in the bank is eliminated. Also some extra saving in mailing timing is provided by the lock-box system as the cheques received in the post office box are not delivered either by the post
office or the firm itself to the bank; rather the bank itself picks them up at the post office.

The lock-box system, as a method of collection of receivables, has a two-fold advantages. They are:

(i) the bank performs the clerical task of handling the remittance prior to deposits, services which the bank may be able to perform at a lower cost.

(ii) the process of collection through the banking system begins immediately upon the receipt of the cheque / remittance and does not have to wait until the firm completes its processing for internal accounting purposes.

METHOD FOR DETERMINING THE LEVEL OF CASH BALANCE

There are various techniques to determine the level of Cash Balance. The most important is the Cash Budget Technique. Cash Budget is an integral part of cash planning. It is prepared on the basis of forecasts of cash inflows and cash-outflows for a given period. The forecast of cash flows are made on the basis of past behaviour of cash flows as modified and adjusted to likely changes
during the coming period. Cash budgets are usually prepared on annual basis for the next operating period.

However, in addition to annual cash budget, monthly, quarterly and six monthly cash budgets can also be prepared for internal management purposes.

Cash budget is like a mirror in which the pattern of future cash flows is reflected. This provides an opportunity to the management to foresee the extent and duration of intermittent phases of cash surplus and ‘cash deficit’ likely to recur during the next operating period.

Over the years, large corporations and business houses succeed in developing in-built skills and foresights to make accurate forecasts of future cash flows and prepare accurate cash budgets.

**CASH MANAGEMENT : FACTORS DETERMINING CASH NEEDS**

The factors that determine the required cash balances are:
Synchronisation of Cash Flows

The need for maintaining cash balances arises from the non-synchronisation of cash perfectly coincide or balance each other, there would be no need for cash balances. The first consideration in determining the cash need is, therefore, the extent of non-synchronisation of cash receipts and disbursements. For this purpose, the inflows and outflows have to be forecast over a period of time, depending upon the planning horizon which is typically a one-year period with each of the 12 months being a sub-period.

Short Cost

Another general factor to be considered in determining cash needs is the cost associated with a shortfall in the firm’s cash needs. The cash forecast presented in the cash budget would reveal periods of cash shortages. In addition, there may be some unexpected shortfalls. Every shortage of cash – whether expected or unexpected involves a cost “depending upon the severity, duration and frequency of the shortfall and how the shortage is covered. Expenses incurred as a result of shortfall are called short costs.” Included in the short costs are:-
(i) Transaction costs associated with raising cash to tide over the shortage. This is usually the brokerage incurred in relation to the sale of some short-term near-cash assets such as marketable securities.

(ii) Borrowing costs associated with borrowing to cover the shortage. These include items such as interest on loan, commitment charges and other expenses relating to the loan.

(iii) Loss of trade-discount i.e. a substantial loss because of a temporary shortage of cash.

(iv) Cost associated with deterioration of the firm's credit rating which is reflected in higher bank charges on loans, stoppage of supplies, demands for cash payment, refusal to sell, loss of firm's image and the attendant decline in sales and profits.

(v) Penalty rates by banks to meet a shortfall in compensating balances.

**EXCESS CASH BALANCE COSTS**

Another consideration in determining cash needs is the cost associated with maintaining excess/idle cash. The cost of having excessively large cash balances is known as excess cash balance cost. If large funds are idle, the implication is that the firm has
missed opportunities to invest those funds and has thereby lost interest which it would otherwise have earned. This loss of interest is primarily the excess cost.

**Procurement and Management**

These are the costs associated with establishing and operating cash management staff and activities. They are generally fixed and are mainly accounted for by salary, shortage, handling of securities, etc.

**Uncertainty and Cash Management**

Finally, the impact of uncertainty on cash management strategy is also relevant as cash flows cannot be predicted with complete accuracy. The first requirement is a precautionary cushion to cope with irregularities in cash flows, unexpected delays in collections and disbursements, defaults and unexpected cash needs.

The impact of uncertainty on cash management can, however, be mitigated through (i) improved forecasting of tax payments, capital expenditure, dividends etc; (ii) increased ability to borrow through overdraft facility.
EVALUATION OF CASH MANAGEMENT PERFORMANCE

Cash is the life blood of any business. It is the most important component of the working capital of any business concern. Cash is the major and much awaited output of the company’s operations.

Cash Management efficiency can be judged in many ways. Whether a business enterprise is keeping enough, more than enough or less than adequate cash can be known by measuring the performance with regard to liquidity and operational objectives.

For the evaluation of the different aspects of cash management performance, the following ratios have been used:

(a) To Test adequacy of cash
   (i) Cash position ratio.

(b) To assess the effective control of cash flows:
   (i) Cash to current assets ratio.
   (ii) growth rate of cash and sales and cash to sales ratio.

(c) For productive utilization of Surplus cash.
   (i) Marketable securities to current assets.
Adequacy of Cash

While planning the management of cash, the two important objectives are kept in focus, they are liquidity and profitability. It is obvious that the cash balance must be proper so that current obligations can be met at right time. There should be no cash-deficit and cash-surplus. Many a time it may so happen that even profit-earning firms are confronted with a poor liquidity problem, while there may be enough surplus cash or liquidity at a given point of time in a firm which is earning a low profit or even no profit. In order to avoid such situations and for timely completion of each operating cycle a careful and meticulous cash planning is must.

In order to test a firm’s liquidity and solvency current and quick ratios are commonly used.

1. **Cash Position ratio** – In the computation of this ratio only the absolute liquid assets are compared with current liabilities. This ratio generally indicates the adequacy of cash for meeting current liabilities. Table 6(E) shows the position of selected textile companies.
Table 6(E)

CASH POSITION RATIO IN THE SELECTED TEXTILE MANUFACTURING COMPANIES IN U.P.
FROM 1998-99 TO 2003-2004
IN TIMES

<table>
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</thead>
<tbody>
<tr>
<td>The British India Corporation Ltd.</td>
<td>0.12</td>
<td>0.23</td>
<td>0.15</td>
<td>0.035</td>
<td>0.35</td>
<td>0.23</td>
<td>0.18</td>
</tr>
<tr>
<td>The Elgin Mills Co. Ltd.</td>
<td>0.050</td>
<td>0.040</td>
<td>0.041</td>
<td>0.049</td>
<td>0.016</td>
<td>N.A.</td>
<td>0.04</td>
</tr>
<tr>
<td>Cawnpore Textiles Ltd.</td>
<td>0.006</td>
<td>0.12</td>
<td>0.13</td>
<td>0.18</td>
<td>0.08</td>
<td>N.A.</td>
<td>0.10</td>
</tr>
</tbody>
</table>

Source: Annual Reports & Accounts of Companies under study.

Table 6(E) shows that the British India Corporation Ltd. had a fluctuating trend in the cash position ratio throughout the study period. It increased to 0.23 times in the year 1999-2000. It decreased in 2000-01 followed by another decrease in 2001-02.
which was 0.035 times. It was 0.35 times in 2002-03 which decreased in 2003-04 to 0.23 times.

The above table reveals that cash position ratio in the Elgin Mills Company Ltd. showed fluctuating trend. It was 0.05 times as compared to 0.04 times in 1999-2000 and 0.041 times in 2000-01.

It increased to 0.049 times in 2001-2002 followed by a decrease in the year 2002-03 which was 0.016 times.

In the case of Cawnpore Textiles Ltd. there was an increasing trend in the ratio throughout the study period. It was 0.006 times in 1998-99 as against to 0.12 times in 1999-2000. It increased in 2000-01 to 0.13 times. In 2002-03 it showed a decreasing trend to 0.08 times as compared to 0.18 times in the year 2001-02.

Control of Cash flows

Every business aim at maximising profitability which can be achieved if the cash resources are fully employed. On the contrary it should economize on cash holdings with impairing the overall liquidity requirements, which can be achieved by an effective higher control over cash flows.
The important ratio show the achievement of the company in this regard:-

i) Cash to current assets ratio.

ii) Growth rate of cash and sales and cash to sales ratio.

1. Cash to current Assets ratio

"Cash is the least profitable of all assets." Therefore, maintaining an unduly heavy amount of cash, which may be much more than the business needs indicates that the management is not able to usefully employ its surplus cash. In other words holding cash is most essential, yet holding more than just enough cash will be a losing proposition for a business firm.

The proportion of cash to total current assets affects the profitability of a concern. The lower the proportion, the greater the profitability. The position of selected textile manufacturing companies in U.P. can be checked out through Table 6(F).

The ratio of the British India Corporation Ltd. marked a fluctuating trend through-out the study period. The ratio increased in the year 1999-2000 to 42.11 per cent as compared to 26.47 per cent in 1998-99. It decreased in 2000-01 to 22.60 per cent. The
ratio was the lowest in 2001-02 being 5.86 per cent. It was 39.54 per cent in 2002-03 and 22.92 per cent in 2003-04. This shows a slack control of the company over cash during the study period.

Table 6(F) depicts that in the Elgin Mills Company Ltd. the ratio was the lowest in 2002-03 being 12.46 per cent and the highest in 1998-99 being 50.72 per cent. It was 45.43 per cent in 1999-2000, 49.99 per cent in 2000-01 and 47.44 per cent in 2001-02. This again indicated slack control of the company over the cash during the study period.
Table 6(F)
CASH TO TOTAL CURRENT ASSETS RATIO
IN THE SELECTED TEXTILE MANUFACTURING COMPANIES IN U.P.
FROM 1998-99 TO 2003-2004

<table>
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<tr>
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</tr>
</thead>
<tbody>
<tr>
<td>The British India Corporation Ltd.</td>
<td>26.47</td>
<td>42.11</td>
<td>22.60</td>
<td>5.86</td>
<td>39.54</td>
<td>22.92</td>
<td>26.58</td>
</tr>
<tr>
<td>The Elgin Mills Co. Ltd.</td>
<td>50.72</td>
<td>45.43</td>
<td>49.99</td>
<td>47.44</td>
<td>12.46</td>
<td>N.A.</td>
<td>41.20</td>
</tr>
<tr>
<td>Cawnpore Textiles Ltd.</td>
<td>1.27</td>
<td>22.28</td>
<td>24.24</td>
<td>43.27</td>
<td>27.82</td>
<td>N.A.</td>
<td>23.77</td>
</tr>
</tbody>
</table>

Source: Annual Reports & Accounts of Companies under study.

In Cawnpore Textiles Ltd. there was marked a fluctuating trend in the ratio of cash to total current assets during period under study. The ratio was 1.27 per cent in 1998-99. It showed
increasing trend in 1999-2000, 2000-01, 2001-02 followed by decrease in 2002-03 to 27.82 per cent.

The above table shows that average ratio of cash to current assets was highest in the Elgin Mills Company Ltd. i.e. 41.20 per cent, followed by the British India Corporation Ltd. at 26.58 per cent, Cawnpore Textiles Ltd. at 23.77 per cent.

ii) GROWTH RATE OF CASH AND SALES AND CASH TO SALES RATIO

Large Cash and bank balance accompany Growth in Sales.

The sound cash management is the one where rate of growth in cash holdings is lower than the growth rate in sales. A downward trend in cash to sales ratio over the years indicates effective control over cash flows. Table 6(G) shows the position of selected textile manufacturing companies in Uttar Pradesh.

Table 6(G) reveals that the British India Corporation Ltd.'s growth rate of cash holding was higher than the rate of growth of sales during the period under study taking the year 1998-99 as base year. Cash balance in the company had gone by 327.75 per cent in
2003-04 and sale had gone up by 221.01 per cent in 2003-04 as compared to 1998-99 as base year. The sales showed decreasing trend in 2002-03.

Table 6(G) reveals that the Elgin Mills Company Ltd. registered a decrease in 1999-2000 and after this in 2000-2001. It showed an increasing trend in 2001-02. Again showed a decreasing trend in 2002-03. The rate of growth in sales marked an increasing trend in 1999-2000. It showed decreasing trend in the remaining years of study period.

In the case of Cawnpore textiles Ltd. there was increasing trend in the rate of growth in cash holding upto 2001-02 and it decreased in 2002-03. The rate of growth in sales was higher in 1999-2000. It showed decrease in 2000-01.

Some data are not available in case of the Elgin Mills Ltd. that is because of the High Court decision of winding-up of company. At the last hearing on 24.7.2000 the High court directed that the stay order dated 13.10.99 shall remain in operation till 18.8.2000.
### Table - 6(G)

**SIZE OF CASH IN THE SELECTED TEXTILE MANUFACTURING COMPANIES IN U.P. AND THEIR VALUE OF TOTAL SALES FROM 1998-99 TO 2003-2004**

<table>
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<tr>
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<tbody>
<tr>
<td><strong>The British India Corporation Ltd.</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>4,60,54,779</td>
<td>8,18,65,842</td>
<td>5,29,85,929</td>
<td>1,26,41,912</td>
<td>18,95,20,043</td>
<td>15,09,44,739</td>
</tr>
<tr>
<td>Trend</td>
<td>100</td>
<td>177.75</td>
<td>115.04</td>
<td>27.44</td>
<td>411.51</td>
<td>327.75</td>
</tr>
<tr>
<td>Sales</td>
<td>6,66,91,282</td>
<td>10,77,45,760</td>
<td>11,36,04,712</td>
<td>15,25,17,666</td>
<td>14,00,17,394</td>
<td>14,74,00,103</td>
</tr>
<tr>
<td>Trend</td>
<td>100</td>
<td>161.55</td>
<td>170.34</td>
<td>228.69</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>The Elgin Mills Company Limited</strong></td>
<td></td>
<td></td>
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<td></td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>3,32,57,459</td>
<td>2,85,47,745</td>
<td>2,83,90,001</td>
<td>3,61,02,162</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trend</td>
<td>100</td>
<td>85.83</td>
<td>85.36</td>
<td>108.55</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>14,49,264</td>
<td>18,28,275</td>
<td>11,88,820</td>
<td>40,476</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trend</td>
<td>100</td>
<td>126.15</td>
<td>82.02</td>
<td>2.79</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Cawnpore Textiles Ltd.</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cash</td>
<td>5,61,933</td>
<td>1,26,02,877</td>
<td>1,36,13,367</td>
<td>2,20,82,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trend</td>
<td>100</td>
<td>2242.77</td>
<td>2422.59</td>
<td>3929.65</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>10,28,872</td>
<td>14,24,111</td>
<td>22,755</td>
<td>-</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trend</td>
<td>100</td>
<td>138.41</td>
<td>2.21</td>
<td>-</td>
<td></td>
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</tr>
</tbody>
</table>

Source:- Annual Reports & Accounts of the Company under study.
In case of Cawnpore textiles where datas are not available, it was declared sick company and would remain open till 18.8.2000.

Table 6(H)

CASH TO SALES RATIO IN THE SELECTED TEXTILE MANUFACTURING COMPANIES IN U.P. FROM 1998-99 TO 2003-2004

<table>
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</tr>
</thead>
<tbody>
<tr>
<td>The British India Corporation Ltd.</td>
<td>69.05</td>
<td>75.98</td>
<td>46.64</td>
<td>8.28</td>
<td>135.35</td>
<td>102.40</td>
<td>72.95</td>
</tr>
<tr>
<td>The Elgin Mills Co. Ltd.</td>
<td>2294.78</td>
<td>1561.45</td>
<td>2388.08</td>
<td>89193.99</td>
<td>-</td>
<td>N.A.</td>
<td>23859.57</td>
</tr>
<tr>
<td>Cawnpore Textiles Ltd.</td>
<td>5.46</td>
<td>884.96</td>
<td>59825.82</td>
<td>-</td>
<td>-</td>
<td>N.A.</td>
<td>20072.08</td>
</tr>
</tbody>
</table>

Source: Annual Reports & Accounts of Companies under study.

It is inferred from the table that the British India Corporation Ltd. showed fluctuating trend in the cash to sales ratio during the study period. It was 69.05 per cent in 1998-99 and 75.98 per cent in 22-2000. It showed decreasing trend in 2000-01 and 2001-02 to 46.64 and 8.28 per cent respectively. Again it showed increasing
trend in 2002-03 and 2003-04 to 135.25 per cent and 102.40 per cent respectively.

According to Table 6(H) the Elgin Mills showed increasing trend in the study period except in 1999-2000.

The Cawnpore Textiles Ltd. also showed increasing trend in the cash to sales ratio during study period.