ISSN NO.2395-0692

IJAHMS International Journal of Arts, Humanities and Management Studies

A Study on Working Capital Efficiency and Profitability of Directus Consultants Pvt, Ltd

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ABSTRACT :

The challenges involved in managing current assets, current liabilities, and the linkages between them are the focus of working capital management. Cash, marketable securities, accounts receivable, and inventories make up the bulk of the company's current assets. In order to maintain a suitable level of working capital inside the organisation, working capital management aims to manage the firm's current assets and current liabilities.

Since their establishment in 2010 in the fields of corporate law, accounting, taxation, labour, and legal services, Directus Consultants Private Limited has been at the forefront of innovation. The team behind Directus Consultants Private Limited and Directus Advisory LLP is made up of seasoned and effervescent experts who are passionate about developing and maintaining company legal compliance and secretarial practises. The company has offices in Trivandrum, Bengaluru, and Chennai in addition to its headquarters in Kochi, Kerala.

This study reviews the literature on working capital efficiency and business profitability. Working capital efficiency assesses how successfully a business balances the amount of money it has invested in inventoried products against the amount it owes for purchasing the inventory. The fundamental goal of working capital management is to keep an eye on a company's assets and liabilities in order to maintain a sufficient cash flow and achieve immediate business objectives.

KEYWORD:- *Component,formatting,style,styling,insert***.**

INTRODUCTION

The impact of working capital management on a company's profitability is the focus of this research study. Working capital management is a crucial component of an organization's operational activities since it directly affects the profitability and liquidity of the business. Profitability and liquidity are two separate aspects of the same concept. A successful company can make sure that it can pay off its short-term debt and effectively manage its cash flow. A company's liquidity shows how well-equipped it is to meet immediate obligations. Working capital is extremely important in this day and age of rising capital expenses and restricted resources. The successful management of a company's working capital is commonly regarded to play a significant role in its profitability.

One of the most important facets of running a day-to-day business is working capital management. Working capital generally looks after the company's current assets, which are the financial resources allocated to the company as it switches from one kind to another throughout daily operations. Current assets come in a variety of forms, but the most prevalent ones are cash, prepaid expenses, short-term investments, accounts receivable, inventories, and other current assets. The goal of optimising working capital balance is to minimise working capital needs while increasing revenue possibilities. Working capital efficiency and a company's profitability are closely related in a linear fashion.

The establishment of Directus Consultants Private Limited took place in 2010. The director is R.I. Gokul. They have pioneered innovations in corporate law, accounting, taxation, labour, and legal services. The business has offices in Chennai, Bengaluru, Trivandrum, and Kochi, all in Kerala. A group of seasoned and emerging experts that are passionate about developing and sustaining business legal compliance and secretarial practises make up Directus Consultants Private Limited and Directus Advisory LLP. Their mission is to support statutory compliance, good practises, and regular compliance audits for our clients, establishing the foundation for sound business expansion. Incomparable quality and accuracy are offered by Directus in its business incorporation services, which are open, efficient, and dependable. They respect a new entrepreneur's needs and make sure the solutions they need are accessible. Its goals are to deliver top-notch services while upholding high standards of loyalty and discretion, as well as to work towards ongoing improvement. In order to meet the client's expectations with the highest discretion, attention, and care, the emphasis is on identifying the client's precise requirements, making sure the work is completed on schedule, and so forth. Among their notable clients are Bharat Petroleum, Terumo Penpol, V-Guard, Eastern, and others. The company's mission is to deliver quality services while upholding high standards of commitment and confidentiality, constantly pursuing continuous learning, and striving to improve. The company's vision is to promote compliance with statutes, healthy practises, and regular compliance check-ups for our clients, laying a strong foundation for healthy corporate growth.

This study examines how profitability and working capital are related using data from the same company. The profitability is inversely correlated with the average collection period, meaning that the shorter the average collection period, the higher the profitability. This implies that a decrease in the amount of time a company must pass before getting payment from sales has an advantageous effect on the company's profitability. Second, there is a highly significant positive correlation between the average payment period and profitability. This implies that the longer a corporation pays its creditors, the more profitable it is. Thirdly, the company will become more profitable as the cash conversion cycle gets shorter. To demonstrate that the company's profitability has been maintained, managers can then provide a positive value for the shareholders.

NEED OF THE STUDY.

The study primarily attempts to close the gap in working capital management in a service industry other than the manufacturing and trade industries. By undertaking the study, the business will have a leg up in assessing how profitable it will be during the epidemic. The management of the company will be able to assess the state of their working capital management and, if there is a gap, take remedial action to make better working capital decisions going forward. The results of this study will contribute to the body of knowledge on working capital management and provide

ISSN NO.2395-0692
International Journal of
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academics with the crucial literature review for future research. Entrepreneurs who want to launch a career in the service sector might use the research as a resource.

RESEARCH METHODOLOGY

Both primary and secondary sources provide the data needed for the analysis. Sales, purchases, and other balance sheet items were among the balance sheet items for which information was gathered from the company's public annual reports and records. The study's research design, which was employed, is purely descriptive. The study gives a description of the firm's makeup, size, and working capital and examines its profitability after managing its working capital.

Graphs have been supplied whenever possible, and the data has been correctly collated. The following are the key analytical and interpreting methods and instruments employed in the study:

- Comparative Balance Sheet.
- Ratio Analysis
- Corelation Analysis

The analysis also employs tables, graphs, and charts.

The analysis's findings list the fundamental needs for working capital, tips for managing an efficient organisation, and information on how working capital influences a company's profitability.

3.1 Population and Sample

The study's research design is descriptive in nature. In addition to describing the firm's structure, size, and working capital, the study examines the firm's profitability following the management of working capital.

3.2 Data and Sources of Data

Both primary and secondary sources provide the data needed for the analysis. Data on sales, purchases, current assets, current liabilities, and other balance sheet elements were gathered from the company's public annual reports and records.

3.3 Theoretical framework

Working capital is the difference between current assets and current liabilities. Managing current assets and current liabilities together is therefore managing working capital. By keeping an eye on and making the most use of a company's current assets and liabilities, working capital management is a business approach used to make sure it runs smoothly. Working capital is used more as a phrase in accounting than as a management concept. For the purposes of definition, there are two notions for working capital: the gross concept and the net concept. According to the gross definition of working capital, it alludes to the company's existing assets. Gross working capital is the entire current assets of the company. Current Assets - Current Liabilities is known as the net idea, sometimes known as net working capital. Therefore, the difference between resources that are currently in cash or are easily convertible into cash (current assets) and organisational commitments for which future cash needs will arise (current liabilities) is the amount of working capital. It is explained as the distinction between current assets and current liabilities.

Characteristics of Working Capital :

Short-Term Needs: Working capital is being used to buy current assets, which will only be transformed into cash for a little time.

Circular Movement: Cash is continually being transformed into working capital, which is then converted back into cash again.

Work still varies from time to time, even if it's something small like your pay.

Being easily convertible into cash at any time without incurring losses, it is exceedingly liquid.

Less Risky: Because current assets, like working capital, are only held for the short term, they carry less risk than long-term investments.

No Need for particular Accounting System: Since working capital is a transient asset that will only last for one year, there is no need to adopt a particular accounting system.

Sources of Working Capital

PERMANENT OR FIXED	TEMPORARY OR VARIABLE
Shares	Commercial paper
Debentures	Indigenous bankers
Public deposits	Trade credit
Ploughing back of profits	Instalment credit
Loans from financial institutions.	Advances

Table 1: Sources of Working Capital

Financing Of Continuous, Stable, Or Long-Term Working Capital

1.Shares : The most crucial way to raise long-term or permanent capital is through the issuance of shares. Shares of a firm can be issued in a variety of forms, including equity shares, preference shares, and deferred shares. However, a public corporation is not permitted to issue deferred shares under the Companies Act of 1956. Preference shares come with preferential rights for dividends paid at a defined rate and for capital return at the company's liquidation. The dividend on equity shares is payable if there are enough earnings available; there is no fixed commitment charge associated with these shares.

2.Debentures : A debenture is a document that a firm issues to acknowledge a debt to a holder. Additionally, it is a significant way to raise ongoing or permanent working capital. The company's creditors are the debenture holders. Debentures have a fixed rate of interest. Debenture interest is charged to the profit and loss statement.

3. Public Deposits : Fixed deposits that a business accepts directly from the general public are known as public deposits. In the absence of banking services, this method of short- and medium-term financing was highly common. Traditionally, the textile businesses in Ahmedabad and Bombay took public deposits for terms of six months to a year. However, business houses now days even accept long-term deposits of 5 to 7 years.

4. Ploughing back of profits : Reinvesting surplus income back into a company's operations is referred to as "plowback profits." The expansion, modernization, replacement, etc. of an established firm are best suited for this internal source of funding. This kind of financing has a lot of benefits: it is the least expensive, or better still, cost-free, source of capital; there is no requirement to own securities; there is no dilution of control; it guarantees a stable dividend policy; and it wins the public's confidence. But an excessive reliance on reinvesting gains could result in monopolies, financial mismanagement, overcapitalization, speculation, etc.

5. Loans from Financial Institutions : Commercial banks, life insurance companies, the Industrial Finance Corporation of India, state financial corporations, state industrial development corporations, the Industrial Development Bank of India, etc. are just a few examples of financial institutions that offer short-, medium-, and long-term loans.

Financing Of Temporary/ Variable Or Short-Term Working Capital

1. Commercial Paper : Short-term capital loans are largely provided by commercial banks. They offer a variety of loans that are specialised to satisfy the unique requirements of enterprises. The various ways that banks typically offer loans and advances include cash credit, overdrafts, the buying and discounting of invoices, and loans.
2. Indigenous Bankers : Prior to the establishment of commercial banks, private money lenders and other local bankers served as the only sources of funding and commanded exorbitant interest rates.
3. Trade credit : In the regular course of business, suppliers offer trade credit.
   • Simple and practical financial instrument
   • Informal and impromptu source of money;
   • Flexible credit that grows with the company.
4. Instalment credit : A loan with an installment payment schedule is called a credit. The borrower consents to make a predetermined number of installments each month in a predetermined amount. A loan with an installment repayment schedule may need several months or perhaps several years to repay.
5. Advances : Advances are given to some company houses by customers and agents in response to orders. This is a source of inexpensive, short-term financing that is employed to reduce working capital expenditures.

Why Is Working Capital Management Essential For Companies?

Working capital is a daily requirement for businesses since they need a consistent quantity of cash to pay bills on time, cover unforeseen expenses, and buy raw materials for manufacturing products. A company's current assets and liabilities should be maintained in a sufficient balance. This is the core objective of working capital management, which is essentially an accounting approach. An efficient working capital management system aids companies in increasing revenue while also helping them meet their financial responsibilities.

Inventory, cash, accounts payable, and accounts receivable management are all aspects of working capital management. Working capital ratios, inventory turnover ratios, and collection ratios are examples of critical performance ratios that may be used by an effective working capital management system to identify areas that need to be prioritised in order to preserve liquidity and profitability.

The main focus of working capital management is to make sure that businesses are using both their assets and liabilities to keep operations running smoothly. This frequently requires careful management across numerous corporate divisions, which may include accounts payable, inventory management, debt management, and revenue collection.

Simply described, it is the difference between a company's current assets and its current liabilities. Your assets in this situation are anything that may be quickly converted into liquid cash within a 12-month period, which frequently includes cash, inventory, and accounts receivable. Effective working capital management puts a lot of emphasis on ensuring that the company can retain the liquidity required to keep the business operating while ideally leveraging assets as investments.

For the following things, working capital is required:

- For the acquisition of supplies, equipment, and
- To cover salaries and
- To accrue daily costs and overhead
- Providing customers with financial options
- Should keep enough spare parts, stocks, and work in progress on hand.

3.4 Statistical tools / Data Analysis Techniques

3.4.1 RATIO ANALYSIS

a) WORKING CAPITAL MANAGEMENT RATIO

A company's current assets and obligations should be monitored and utilised to the fullest extent possible as part of working capital management to ensure smooth operations. The efficiency of working capital management can be evaluated using ratio analysis.

1. The current ratio

The current ratio, a critical indicator of a company's financial health, demonstrates its capacity to meet its short-term financial obligations. Though data vary by industry, a working capital ratio below 1.0 generally denotes that a company is having trouble meeting its short-term obligations. Ideal working capital ratios range from 1.2 to 2.0; however, if the ratio exceeds 2.0, it may mean that the company is not maximising the use of its resources to increase sales. The company may not be managing its working capital well if the ratio is high. This is how the current ratio is stated:

Current Ratio = Current Assets / Current Liabilities

2. Working capital turnover ratio

The working capital turnover ratio demonstrates the efficiency with which a company generates sales relative to its working capital. Working capital is the amount that separates a company's current assets from its current obligations. It is a reliable indicator of excessive and insufficient trading. This percentage illustrates how the firm's net working capital has changed across the Working capital The turnover ratio is presented in the following way:

Working Capital Turnover Ratio = Net Sales/Working Capital.

b) PROFITABILITY RATIOS

A group of financial metrics known as profitability ratios are employed to assess a company's propensity to make profits over time in proportion to its revenue, operational expenses, balance sheet assets, and shareholders' equity. Profitability ratios can be contrasted with efficiency ratios, which consider how successfully a company uses its internal resources to generate income.

1.Net Profit Ratio

Based on an inclusive view of profit, the net profit ratio is calculated. After operational as well as non-operational expenses and incomes, it links revenue from operations to net profit. As follows is the calculation:

Net Profit Ratio = Net Profit/Revenue from Operations × 100

2. Return on Assets

The return on assets ratio evaluates the firm's profitability in relation to the assets that are used by the company. The ROA may be calculated using the following notions of assets and net profit (return):

Return on Assets = Net Income/Total Assets

3. Return On Equity

Return on equity is a metric used to assess a company's capacity to profit from equity investments. This ratio demonstrates how profitably the company has utilised the owner's capital. It also calculates the equity shareholders' % return.

Return on Equity = Net Income/Shareholder's Equity

c) Leverage Ratios

Leverage ratios are one of many financial metrics that evaluate a company's capacity to satisfy its financial obligations or how much money is obtained through debt (loans). Because businesses typically employ a combination of debt and equity to fund their operations, the leverage ratio category is crucial. Knowing how much debt a company has can help determine if it will be able to pay off its loans when they are due.

1.Debt-Equity Ratio

The debt-to-equity ratio, a measure of leverage, determines how much overall debt and financial liabilities weigh against total shareholders' equity. The D/E Ratio employs total equity instead of total assets, which is the denominator in the debt-assets ratio. This ratio shows the lean of a company's capital structure towards debt or equity financing.

Debt to Equity Ratio = Total Debt / Shareholders' Equity

3.4.2 Correlation Analysis

- H01: There is a no relationship between the current ratio and certain selected profitabilityratios

- H02: There is no relationship between the Working capital turnover ratio and certain selectedprofitability ratios
- H03: There is no relationship between the Debt Equity ratio and certain selected ROA
- H04: There is no relationship between the Debt Equity ratio and certain selected ROE

To determine the extent to which working capital is linked to profitability, Karl Pearson's correlation coefficients between a few selected working capital management ratios and the selected ratios pertaining to profitability are employed.

For the purpose of data analysis, a number of important ratios related to working capital management and the ratios that are important to evaluate profitability have been calculated using the information provided by Directus Consultancy Private Ltd. Ratios such as the Working Capital Turnover Ratio (WCTR), Current Ratio (CR), Net Profit Ratio (NPR), Return on Equity (ROE), and Return on Assets (ROA) have all been used to show how well working capital is managed. Working capital management and profitability have been correlated to varying degrees, according to Pearson's simple correlation coefficient.

Calculation of Correlation Matrix of WC and Profitability Ratios

	GPR(X1)	*NPR(X2)*	*ROA(X3)*	*ROE(X4)*	*CR(Y1)*	*WCTR(Y2)*
GPR(X1)	**1**	**0.8710341**	**0.854001757**	**0.087127799**	**-0.31255732**	**0.300185288**
P-value	**0**	**0.0239**	**0.0304**	**0.8696**	**0.5464**	**0.5632**
NPR(X2)	**0.8710341**	**1**	**0.97245646**	**0.561859317**	**-0.042959389**	**-0.147377622**
P-value	**0.0239**	**0**	**0.0011**	**0.2459**	**0.9356**	**0.7805**
ROA(X3)	**0.854001757**	**0.97245646**	**1**	**0.52470709**	**0.124828069**	**-0.233852364**
P-value	**0.0304**	**0.0011**	**0**	**0.2852**	**0.8137**	**0.6556**
ROE(X4)	**0.087127799**	**0.56185932**	**0.52470709**	**1**	**0.364155025**	**-0.762142689**
P-value	**0.8696**	**0.2459**	**0.2852**	**0**	**0.4779**	**0.0781**
CR(Y1)	**-0.31255732**	**-0.04295939**	**0.124828069**	**0.364155025**	**1**	**-0.865312221**
P-value	**0.5464**	**0.9356**	**0.8137**	**0.4779**	**0**	**0.026**
WCTR(Y2)	**0.300185288**	**-0.14737762**	**-0.23385236**	**-0.76214269**	**-0.865312221**	**1**
P-value	**0.5632**	**0.7805**	**0.6556**	**0.0781**	**0.026**	**0**

$$r = \frac{n\sum xy - (\sum x \sum y)}{\sqrt{[n\sum x^2 - (\sum x)^2][n\sum y^2 - (\sum y)^2]}}$$

	CR	WCTR	NPR	ROA	ROE
CR	1				
WCTR		1			
NPR		-0.14738	1		
ROA	0.124828069	-0.23385		1	
ROE	0.364155025	-0.76214			1

- The correlation coefficient between CR and ROA is 0.124 which shows a weak positivecorrelation.
- The correlation coefficient between CR and ROE is 0.364 which shows a weak positivecorrelation.
- The correlation coefficient between WCTR and NPR is -0.147 which is weakly negativelycorrelated.
- The correlation coefficient between WCTR and ROA is -0.233 which implies that a weaknegative correlation exists between the two variables.
- The correlation coefficient between WCTR and ROE is -0.762 which possesses almost a strong negative correlation.

3.4.3 COMPARATIVE BALANCE SHEET

A comparative balance sheet is a statement that displays an organization's financial situation throughout several time periods for which comparison is made or is necessary. The financial status is contrasted between two or more time periods in order to illustrate the pattern and direction of change, examine it, and take appropriate action.

IV. RESULTS AND DISCUSSION

ISSN NO.2395-0692
IJAHMS International Journal of Arts, Humanities and Management Studies

From the discussion with the company officials, it has been found that, as the firm operates mainly with legal services and unavoidable audit and documentation purposes of the client companies, the impact of pandemic has been efficiently managed through online platforms.

i. The firm has satisfactory level of Working Capital.
ii. Higher turnover ratios of the firm reflect efficient utilisation of resources resulting inhigher liquidity and profitability in the business.
iii. As the net profit ratios are in the ideal range, the company generates adequate level ofprofit.
iv. The Return on Equity values are high and so the company is able to grow without largecapital expenditures.
v. The Return on Assets shows that the firm is successful at making a profit of its currentassets.
vi. There exists a negative relationship between the profitability ratio NPR and the workingcapital turnover ratio WCTR.
vii. There exists a moderate degree of positive correlation between the working capital turnover ratio WCTR and the profitability ratio ROE.
viii. There exists a weak negative correlation between WCTR and ROA.
ix. There exists a weak positive correlation between the working capital management ratioCR and the profitability ratios ROA and ROE.
x. There exists a weak negative correlation between Debt-Equity and ROA
xi. There exists a strong negative correlation between Debt-Equity and ROE.
xii. There is a decrease in net profit of Rs.65,687.32 (26%) in the financial year 2017-2018, Rs.29,990.33 lakhs (6%) in the financial year 2019-2020 and Rs.4,38,697.12 lakhs (88%)in the financial year.

Regardless of whether a sector is manufacturing- or service-based, working capital is the lifeblood of every industry. The primary and most crucial requirement for running a firm on a daily basis is working capital. The business receives much-needed liquidity through working capital. Working Capital Finance lowers the total amount of funds needed to develop Current Assets, which enhances the turnover ratio. We discovered a substantial correlation between net operating profitability and liquidity as well as a favourable correlation between effective working capital management and firm profitability. Based on the aforementioned data, we may draw the conclusion that if the companies manage their working capital in ways that are more effectively, these results (findings) can be strengthened even more. Management of Working Capital refers to "managing the current liabilities and the financing of the current assets." The effectiveness of the working capital and the profitability of this firm are assessed in this study using three key tools. Ratio analysis, correlation analysis, and comparative balance sheets are three of them. In assessing a company's performance, working capital management may be of crucial relevance. Companies' management systems will become more profitable in the long run if they handle their cash, accounts receivable, and inventories well. As a result, the working capital management system at Directus is effective.

ISSN NO. 2395-0692
International Journal of
Arts, Humanities and Management Studies

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