IMPACT OF WORKING CAPITAL MANAGEMENT ON THE PROFITABILITY OF MANUFACTURING COMPANIES LISTED ON THE NIGERIAN STOCK EXCHANGE

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By

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ABSTRACT

Working capital management refers to the management of the short-term assets of a business. It is very important and plays a vital role for firms' profitability. In spite of its importance, there is a serious dearth of literature on working capital management and profitability especially in sub-Saharan Africa, particularly Nigeria. Therefore, the objective of this study is to investigate the impact of working capital management on the profitability of the manufacturing companies listed on the Nigerian Stock Exchange. Panel data methodology was employed to test this relationship with both the fixed and the random effects estimation techniques. Accordingly, all the manufacturing companies on the Nigerian Stock Exchange totalling 55 were drawn as the sample and the study was conducted for five years (2008-2013). Data were obtained from the financial statements of the companies through the Securities and Exchange Commission. Findings from the panel data regression analysis revealed that average collection period and inventory conversion period were significantly negatively related to profitability, which suggests that the shorter the periods the higher the profitability of the manufacturing companies. However, average payment period was positively and significantly related to profitability, depicting that the longer the period, the higher the profitability. The debt ratio and other current liabilities to the total assets ratio were not significantly related to profitability. Finally, the study provides managerial implications and the direction for future research.

Keywords: working capital management, Nigerian Stock Exchange, profitability, Nigeria.

ABSTRAK

Pengurusan modal kerja merujuk kepada pengurusan aset-aset jangka pendek sesebuah perniagaan. Aset-aset ini sangat penting dan memainkan peranan yang besar dalam menentukan keberuntungan sesebuah firma. Sungguhpun demikian, masih terdapat kekurangan yang serius bagi literatur dalam bidang pengurusan modal kerja dan keuntungan, terutamanya di kawasan sub-Sahara Afrika, khususnya di Nigeria. Justeru, objektif kajian ini adalah untuk menyiasat kesan pengurusan modal kerja ke atas keuntungan syarikat-syarikat pembuatan yang disenaraikan di Bursa Saham Nigeria. Kaedah data panel telah digunakan untuk menguji hubungan ini dengan kedua-dua teknik penganggaran kesan tetap dan teknik penganggaran kesan rawak. Semua syarikat pembuatan di Bursa Saham Nigeria yang berjumlah 55 buah telah dipilih sebagai sampel dan kajian telah dijalankan selama lima tahun (2008-2013). Data diperoleh daripada penyata kewangan syarikat melalui Suruhanjaya Sekuriti dan Bursa. Hasil analisis regresi data panel mendedahkan bahawa tempoh kutipan purata dan tempoh penukaran inventori mempunyai hubungan negatif yang signifikan dengan keuntungan, yang mencadangkan bahawa lebih pendek kitaran, semakin tinggi keuntungan syarikat-syarikat pembuatan ini. Walau bagaimanapun, tempoh purata pembayaran didapati mempunyai hubungan positif yang signifikan dengan keberuntungan. Hal ini memberi gambaran bahawa semakin lama tempoh purata pembayaran, maka akan lebih tinggi keuntungan syarikat. Nisbah hutang dan nisbah liabiliti semasa lain kepada jumlah aset didapati tidak mempunyai hubungan yang signifikan dengan keberuntungan. Akhir sekali, implikasi pengurusan dan hala tuju kajian akan datang turut dikemukakan dalam kajian ini.

Kata kunci: pengurusan modal kerja, kitaran penukaran tunai, keberuntungan, Nigeria.

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LIST OF ABBREVIATIONS

ACP	Average Collection Period
APP	Average Payment Period
CATAR	Current Asset to Total Asset Ratio
CCC	Cash Conversion Cycle
CLTAR	Current Liabilities to Total Asset Ratio
DR	Debt Ratio
FE	Fixed Effect
GOP	Gross Operating Profit
ICP	Inventory Conversion Period
MVA	Manufacturing Value Added
NETOPR	Net Operating Profit
NLS	Natural Logarithm of Sales
NSE	Nigerian Stock Exchange
OC	Operating Cycle
RE	Random Effect
ROA	Return on Assets
SEC	Securities and Exchange Commission
UNIDO	United Nations Industrial Development Organization
WCM	Working Capital Management

CHAPTER ONE

INTRODUCTION

1.1 Background of Study

Literature relating to corporate finance have centered mostly on long-term financial decisions, mainly on investment decisions, company valuations, capital structure and dividends (Afza & Nazir, 2007). The short-term assets and liabilities are important components of total assets and therefore needs to be carefully analyzed (Afza & Nazir, 2007). In view of their importance, there is the need for careful and systematic investigation of these short term assets and liabilities, since they play a vital role for firm`s profitability, risk, as well as its value (Smith, 1980).

Efficient and effective management of working capital is an important component of overall corporate strategy to create the shareholder`s value. Firms try to keep an optimal level of working capital that maximizes the value (Deloof, 2003; Howorth & Westhead, 2003; and Afza & Nazir, 2007). In line with this, working capital management has become one of the most important issues in the organizations (Lamberson, 1995).

Therefore, working capital and its importance is unquestionable (Fillbeck & Krueger, 2005). It directly influences the liquidity and profitability of firm (Raheman & Nasr, 2007). Excellent management of working capital decreases the dependence on external financing due to increased cash flow, thus lowering the chances of default for an organization (Deloof, 2003).

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