LITERATURE REVIEW

While the performance levels of small businesses have traditionally been attributed to general managerial factors such as manufacturing, marketing and operations, working capital management may have a consequent impact on small business survival and growth (Kargar and Blumenthal, 1994).

Working capital starvation is generally credited as a major cause if not the major cause of small business failure in many developed and developing countries (Rafuse, 1996). The success of a firm depends ultimately, on its ability to generate cash receipts in excess of disbursements. The cash flow problems of many small businesses are exacerbated by poor financial management and in particular the lack of planning cash requirements (Jarvis et al, 1996).

Peel and Wilson (1996) have stressed the efficient management of working capital, and more recently good credit management practice as being pivotal to the health and performance of the small firm sector. Along the same line, Berry et al (2002) finds that SMEs have not developed their financial management practices to any great extent and they conclude that owner-managers should be made aware of the importance and benefits that can accrue from improved financial management practices. The study conducted by De Chazal Du Mee (1998) revealed that 60% enterprises suffer from cash flow problems. Narasimhan and Murty (2001) stress on the need for many industries to improve their return on capital employed (ROCE) by focusing on some critical areas such as cost containment, reducing investment in working capital and improving working capital efficiency.

Smith and Begemann 1997 emphasized that those who promoted working capital theory shared that profitability and liquidity comprised the salient goals of working capital management. The problem arose because the maximization of the firm's returns could seriously threaten its liquidity, and the pursuit of liquidity had a tendency to dilute returns.
Smith and Begermann (1997), in their study of industrial companies listed in the Johannesburg Stock Exchange, indicated that current liabilities divided by funds flow (a working capital leverage ratio) displayed the greatest association with return on investment. On the other hand, other indicators like current and quick rations displayed no association.

Shin and Soenen, (1998) highlighted that efficient Working Capital Management (WCM) was very important for creating value for the shareholders. The way working capital was managed had a significant impact on both profitability and liquidity.

Deloof, (2003) discussed that most firms had a large amount of cash invested in working capital. It can therefore be expected that the way in which working capital is managed will have a significant impact on profitability of those firms. Using correlation and regression tests he found a significant negative relationship between gross operating income and the number of days accounts receivable, inventories and accounts payable of Belgian firms.

Ghosh and Maji, (2003) in this paper made an attempt to examine the efficiency of working capital management of the Indian cement companies during 1992 – 1993 to 2001 – 2002. For measuring the efficiency of working capital management, performance, utilization, and overall efficiency indices were calculated instead of using some common working capital management ratios.

The recent work of Howorth and Westhead (2003), suggest that small companies tend to focus on some areas of working capital management where they can expect to improve marginal returns. For small and growing businesses, an efficient working capital management is a vital component of success and survival; i.e both profitability and liquidity (Peel and Wilson, 1996). They further assert that smaller firms should adopt formal working capital management routines in order to reduce the probability of business closure, as well as to enhance business performance. The study of Grablowsky (1976) and others have showed a significant relationship between various success measures and the employment of formal working capital policies and procedures. Managing cash flow and cash conversion cycle is a critical component of overall
financial management for all firms, especially those who are capital constrained and more reliant on short-term sources of finance (Walker and Petty, 1978; Deakins et al, 2001).

On the other hand, it is possible to claim that the most popular measure of working capital management is the Cash Conversion Cycle (CCC). The CCC refers to the number of days between the expenditure of the firm’s cash for the purchase of raw materials and the collection of cash from sales (Sathyamoorthi and Wally-Dima, 2008). Deloof (2003) investigates the relationship between working capital management and firm profitability by using CCC as a measure of working capital management.

Eljelly, (2004) elucidated that efficient liquidity management involves planning and controlling current assets and current liabilities in such a manner that eliminates the risk of inability to meet due short-term obligations and avoids excessive investment in these assets.

Filbeck G. et al. (2005) investigated the data of 26 industries by taking the data of 970 companies during 1996 to 1999. They found out that firms are able to decrease financing cost and/or augment the funds obtainable for development by reduce the amount of funds attached to the current assets.

Lazaridis and Tryfonidis (2006) find a negative relationship between profitability and CCC for 131 listed companies listed in Athens Stock Exchange for the period 2001 - 2004. Similar to the results of these studies focused on large firms, the findings of Garcia-Teruel and Martinez-Solano (2007) also indicates negative relationship between profitability and CCC for small and medium sized firms from Spain.

Sayaduzzaman MD. (2006), examined that the management of British American Tobacco is highly reasonable due to the constructive cash inflows, designed approach in running the major components of working capital by evaluating five years data from 1999-2000 to 2002-2003.

Ganesan (2007) used a sample of 349 telecommunication equipment companies covering the period 2001-2007. The independent variables used were current ratio,
day’s receivable, day’s inventory, day’s payable, day’s working capital and cash conversion efficiency.

**Lazaridis and Tryfonidis (2006)** accounts payable has positive relationship. No conflict between the authors regarding leverage and/or debt financing with negative relationship. Finally, the variable cash conversion efficiency was used by only one author (*Ganesan, 2007*) and presents no association at all with profitability.

**Raheman and Nasr (2007)** selected a sample of 94 listed Pakistani companies from different sectors of economy for a period of 8 years, from 1999-2004. The independent variables used were current ratio, day’s receivable, day’s inventory, days payable and cash conversion cycle.

**Teruel and Martinez–Solano (2007)** also provided the empirical relationship between both the variables. They chose the small and medium sized Spanish firms, a sample of about 8872 small to medium sized enterprises for 1996 to 2002.

In **Christopher and Kamalavalli (2009)** study, they investigated a sample of 14 corporate hospitals in India using panel data analysis for the period 96/97 to 2005/06. The independent variables used were current ratio, quick ratio, inventory turnover ratio, working capital turnover ratio, and debtor’s turnover ratio, ratio of current asset to total asset, ratio of current asset to operating income, comprehensive liquidity index, net liquid balance size, leverage and growth.

**Mathuva (2009)** studied the impact of working capital management on the performance. He took almost 30 listed firms as a sample and all these companies were listed in Nairobi stock exchange and the data was taken from 1993 to 2008.

**Sen. M (2009)** examined the ISE (Istanbul Stock Exchange) listed firms and checked out the relationship with the working capital. According to them there is negative relationship among variables. His research uncovered the importance of the finance directors who act as moderators or catalysts to increase the productivity of the firm in other words they positively affect the firm’s performance.
Zariyawati et al. (2009) investigate the relationship between CCC and profitability for the Malaysian firms for the period 1996-2006 and Dong and Su (2010) analyze the same relationship for the listed firms in Vietnam stock market for the period 2006-2008. And their findings are consistent with the similar studies.

A study by Amarjit Gill 1, Nahum Biger 2, Neil Mathur 3 (2010), under the title "The Relationship between Working Capital Management and Profitability: Evidence from the United States", the aim of this paper is to find the relationship between working capital management and profitability. A sample of 88 American firms listed on New York Stock Exchange for a period of 3 years from 2005 to 2007 was selected.

A study by Huynh Phuong Dong (2010), under the title "The Relationship between Working Capital Management and Profitability: A Vietnam Case", The aim of this paper is based on secondary data collected from the listed firms in Vietnam stock market for the period of 2006-2008 with an attempt to investigate the relationship existing between profitability, the cash conversion cycle and its components for listed firms in Vietnam stock market.

Dong (2010) reported that the firms’ profitability and liquidity are affected by working capital management in his analysis. Pooled data are selected for carrying out the research for the era of 2006-2008 for assessing the companies listed in stock market of Vietnam.

Mohammad Neab and Noriza BMS (2010) worked on crating the relationship between Working Capital Management (WCM) and performance of firms. For their analysis they chose the Malaysian listed companies. They administered the perspective of market valuation and profitability. They used total of 172 listed companies from the databases of Bloomberg.

Saswata Chatterjee (2010) focused on the importance of the fixed and current assets in the successful running of any organization. It poses direct impacts on the profitability liquidity. There have been a phenomenon observed in the business that most of the
companies increase the margin for the profits and losses because this act shrinks the size of working capital relative to sales.

A study by **Ikramul Haq, Muhammad Sohail, Khalid Zaman and Zaheer Alam (2011)**, under the title "The Relationship between Working Capital Management and Profitability: A Case Study of Cement Industry in Pakistan", The result concludes that there is a moderate relationship between working capital management and profitability in the specific context of cement industry in Pakistan.

A study by **Mohammad Alipour (2011)**, under the title "Working Capital Management and Corporate Profitability: Evidence from Iran", the results of the research show that in the studied companies, there is a significant relation between working capital management and profitability and working capital management has a great effect on the profitability of the companies and the managers can create value for shareholders by means of decreasing receivable accounts and inventory, World Applied Sciences Journal 12 (7): 1093-1099, 2011.

A study by **Mamoun M. Al-Debi'e (2011)**, under the title, "Working Capital Management and Profitability: The Case of Industrial Firms in Jordan", the aim of this paper is to examining the relationship between profitability and working capital management measures for industrial companies listed on Amman Stock Exchange in Jordan during the period 2001-2010.

A study by **Talat Afza and Mian Sajid Nazir (2011)**, under the title "Working Capital Management Efficiency of Cement Sector of Pakistan", the aim of this paper is to test the speed of achieving the target level of efficiency by an individual firm during the period of study using industry norms as the target level of efficiency. Findings of the study indicate that the cement sector as a whole did perform well during the study period.