Need for Working Capital Management with Special Reference to Rubber Industry

DISSERTATION SUBMITTED IN PARTIAL FULFILMENT OF THE REQUIREMENT FOR THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION

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Dedicated

to

My Mother
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It is my utmost duty to pay the warmth of thanks to all the obligatories. The persons with those this work interacted from its first word to the last alphabete are the sole creator and inspirator for my efforts to bring out such a huge published work. Among these who become everlasting in the memories are Dr. Najmul Hasan, my supervisor whose invaluable guidance always give me the last hope of survival. My close friends M/s Arif Husain, Mohd. Saleem, Prakash, Arshad and Ishtiaq Ahmad Khan have a lot contribution in the completion of this work.

For the inspiration by my brother Dr. Anwar Habib, I owe my sincere indebtedness.

( ZUBAIR ALAM )
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INTRODUCTION

This dissertation has been written by me as a requirement for Master of Business Administration. The present dissertation 'Need for Working Capital Management with Special Reference to Rubber Industry' has been written keeping in view the growing importance of working capital in the Rubber Industry. At present every industry is facing the problem of arranging working capital. The emphasis is given on the requirements of working capital in the area of particularly in Cash Management, Management of Receivable and Management of Inventories. Due to light money market it is not very easy to get working capital. In this work I have established mainly on inventory management as the major funds are blocked in the inventories and raw material. By using more flexible inventory management we can meet out the funds requirements by our own resources. Moreover, return on investment can be increased by reducing the volume of working capital at the same level of output. In Rubber Industry raw materials are very costly and needs huge investment. With the increased importance of working capital management in mind the work is approached with the awareness that at least it should contribute same thing to Rubber Industries.
Methodology: The methodology adopted for this is by collection of facts from ABC Rubber Co., Ltd. Watching their problems in area of inventories and Receivables I have incorporated my suggestions which will help the industry to maintain their working capital requirements and all the time they will not have to run to the banks and financial institutions for the funds the reference have also been taken from various journals books and periodicals to explain the theoretical part of the project.
WORKING CAPITAL MANAGEMENT

INTRODUCTION:

Scarcity of resources set limits to what management can do. And best utilization of resources is possible only by availing the opportunities. Again more important is goal oriented utilization of resources. The action of all departmental managers, including finance should cause that they are helping in achieving the objective of the firm that is maximisation of value of the firm. Finance is the back-bone of industry and very scared resource. And management of finance has more importance than any other. Any industry whether it is small or big needs capital of two types i.e. (1) Long term of fixed capital and (2) short term or working capital.

(1) **Long Term or Fixed Capital:** This capital is required for long period investment. As it is required for the acquisition of fixed assets such as land, building, plant and machinery required by new industries to make a start and by the established concerns for the purpose of expansion, replacement modernisation and betterment or improvement.

(2) **Short Term or Working Capital:** This is required to finance floating assets like inventory (stock of raw materials...
including stores and other items used in the process of manufacturing, stock-in-process and finished goods), receivable, loans and advances and to provide funds for day-to-day needs.

What is working capital:

Working capital in simple terms is the amount of funds which a company must have to invest for its day-to-day operations. It can also be considered as that portion of the company's total capital which is employed in short-term operations. Now the question arises whether this amount should all the times be available in the form of cash or not. Practically, it is not necessary to keep the funds in cash form at all times. It can take the form of near cash assets or even assets a little farther from cash but yet in the process of moving towards the cash form in a short period. Such items are stocks of raw material and supplies needed for manufacturing, work-in-process, finished goods awaiting sale, sundry good debtors, short-term investment, and money at short notice or money at call.

Concept of Working Capital:

There are two opinions about working capital concept - one is the 'gross' concept and the other is 'net' concept. The financial concept is 'gross concept'. The gross working capital also known as circulating capital, is represented by the sum total of all current assets (convertible in cash with in a period of near one year) of the enterprises. The second is
the 'accounting' concept which is 'net concept'. The net working capital is the difference between current assets and current- liability. These two concepts are not to be regarded as mutually exclusive. Each has its relevance in specific situation.

Current assets comprises items which can be converted into cash in the short run, say within a year, or within the normal operating cycle of the business. Current liabilities are expected to fall due or mature for payment in a short period generally within a year and represent short-term sources of funds. In above opinion there is no consideration of time although the volume of working capital differs from time to time. In busy season more working capital is needed as fixed capital remains same. It the working capital has been classified with a view of time as "Permanent Working Capital and "Variable or Temporary Working Capital". Permanent Working Capital is that amount which represent the current asset required for lowest production on a continuing basis over the entire year.

Variable or Temporary Working Capital is that amount which represent the current additional assets. Seasonal or Cyclical business need more variable working capital.

Definition of working capital given by the Accounting Principles Board of the American Institute of Certified Public Accountants, U.S.A.
"Working capital, sometimes called net working capital, is represented by the excess of current assets over current liabilities and identifies the relatively liquid portion of total enterprise capital which constitutes a margin or buffer for maturing obligations within the ordinary operating cycle of the business*.

In summary, the gross and the net working capital concepts present to distinct and important facts of working capital management. There is no standard fixed what amount of gross or net working capital an enterprise needs. Nor is there any commitment to specific mix or piece-meal financing tied to particular class of assets. There is no stipulation that short-term uses should be wholly financed by short-term sources. It is also not feasible in practice.

Every company has its own constraints and plans giving rise to individual working capital problems and the available data have to be identified and analysed to aid proper decisions. The most important aim is to maintain a proper balance between the magnitude of working capital and the general scale of operations of the company which calls for constant vigilance and coordination of an extensive range of decisions.

Working Capital Management:–

Working capital or circulating capital or current assets of any firm forms a sizable part of its total investment. Management of the funds committed to working capital, therefore, assumes as much importance if not more as any other fixed
investment in the firm. Practically, it has been observed that it is easy to arrange funds for putting up a new industry but it is very hard to arrange and control working capital for the constant running of the industry. Successful running of industry mainly depend upon arrangement and control of working capital through out the life of the firm. Many of the firms have failed only with a reason that there was no proper control on the working capital. To arrange finance is not easy particularly in a country like India where ther is controlled economy. The management of the working capital is one of the major fields in financial management. The aspects of management of working capital are:

1. Determining the Requirements of Working Capital:— It is difficult to set quantitative amounts of working capital for individual firm. We have to consider various factor when determin the requirement of working capital e.g. Nature of business, Manufacturing Policies, Production Process, Growth and expension of business, Turn-over, Business fluctuation and variations, Devident policies, style of purchase and sales, Financial growth and Export and Import policies of government.

2. Financing the Requirements:— Funds to finance the working capital can be obtained through long term sources or short term credit. The three important factors are to be considered when we consider to use long term or short term funds for financing current assets: Flexibility, cost and risk.
3. **Efficient Funds Utilisation Relating to Working Capital:**

Last and most important task involve in efficient working capital management is the use of working capital. Unnecessary investment or untimely expenses results into more of working capital which ultimately reduce the value of profit.

**CASH MANAGEMENT:**

One of the main tasks of financial management is to hold and maintain an adequate, but no excessive cash position. Cash is an obvious and inescapable input into company's operations and as such it has to be available in sufficient doses according to needs on a continuing basis. Cash is also the major and much awaited output or result of the company's operations and there is the need for effective plan to deploy this liquid resource to utmost productive use.

A company that is growing fast and even turning out handsome profits may be continuously faced with a state of shortage of cash and a threat to the uninterrupted flow of production. So, finding adequate funds for operating needs is a perennial preoccupation for the company's finance manager. Paucity of cash, even on a temporary phase, is a source of trouble to most enterprises. Nor is it wise to have, on the average, a lot of cash, which is not an earning asset. Hence the importance of good cash management.
Why hold cash?

According to the eminent British economist, Lord Keynes, the desire to hold cash can be attributed to one or more of the three motives:

1. The transaction motive
2. The precautionary motive
3. The speculative motive

1. The Transaction Motive:— The transaction motive arises from the need for ready funds to make payment failing due in the ordinary course of day-to-day business, such as payment for purchases, payment of wages, payment of operating expenses and payment of taxes and dividends. The operating needs have to be promptly met and any delay will hamper production and profitability. Imagine the lot of the finance manager who has not planned for the necessary funds to pay the annual bonus and suddenly finds himself compelled to raise substantial funds. Payments of taxes and dividends may raise serious problems, in the absence of proper resources planning. Many are the votaries of management by crisis, who repeatedly plead with creditors to bear with them patiently until they manage to find the resources to meet the liabilities. The aim of effective cash management is to ensure smooth functioning of day-to-day business, by judicious direction of the flow of cash into and out of the business, so that the operating and contractual payments are promptly made.
The Precautionary Motive:— The precautionary motive comes from a desire to keep a cash cushion or buffer to meet unexpected contingencies. The degree of precaution will normally bear an universe relationship to the degree of predictability of cash flows of the business. As a matter of abundant caution, many companies had learnt the art of 'cultivating the rich uncle', by establishing and maintaining good lasting link with progressive banking institutions. Ready borrowing power is the best antidote to emergency cash drains and facilitates release of available cash resources for remunerative applications. Where considered advisable, part of the precautionary balance can also be held in the form of near money assets, especially marketable securities.

The speculative motive covers instances where the intention is to hold cash to be able to take advantage of shifts in security prices, arising from changes in interest rates and other factors. This is not a common feature of corporate financial management, except in regard to finance and investment companies.

How Much to Hold?

What are the factors that influence the quantum of transaction and precautionary balances to be held? The following can be mentioned:

1. The expected net cash flows based on the cash forecasts, taking note of the long-range and short-term
cash needs of the company.

2. Expectations as to the degree of possible deviations from forecasts. To anticipate changes in cash flows under varying circumstances, the probability concept can be applied.

3. The maturity scheduled or the structure of the different liabilities of the company.

4. The facility of readily drawable borrowing power in times of emergency.

5. Management's views and attitudes in the matter of liquidity risks, varying between caution and adventure.

CASH PLANNING:

The pursuit of everyday transactions of a company generates cash inflows and outflows. Granting that operations are carried out efficiently and successfully, presenting a long-run pattern of accumulation of cash from current operations. The short-run course, however, will not be smooth and steady and will be symbolised by a variety of pressures and fluctuations which may be attributed to seasonal factors, unexpected market turns, production problems or financing difficulties. Within the operating year, cash surpluses or cash deficits may appear and reappear, at varying points of time, posing borrowing and investing problems, "one may well imagine the adjustment difficulties created by way of life involving frequent changes
between playing the millionaire and playing the pauper, so it is with a corporation that finds itself varying between cash surpluses and deficiencies". If the swings are steep abrupt, financial problems get aggravated. Financial planning can be directed to see that the fluctuations are smooth and gradual, by effective coordination of the inflows and outflows of cash.

If the finance manager finds himself in the unenviable position of having to overcome a sizeable cash shortage, his action has to be instant and, oftentimes, expensive. He has no time to consider several alternatives before deciding on an appropriate course of action. On the other hand, he has to rush out and borrow the money, may be, at an enhanced price. But, if the same cash shortage, at that point of time was anticipated earlier, in the course of scrutiny of cash forecasts, he has some options open before him. He may even decide against borrowing and may find the resources by rearranging some phases of the operating cycle, such as, deferring payments of bills, speedier collection of cut-standings, postponing certain discretionary expenses or by a combination of these measures.

The short-run financial management is built around its two prime and inter-related ingredients, profit and cash management. The objective of cash planning is to provide advance signals as to:
1. What are the amounts of cash that are needed to attain short-run profit objective?

2. How much of these cash requirements can be met out of the cash generated from current income?

3. What are the magnitudes of the ebbs and flows of cash emanating from operations, and what are the sizes and frequencies of the resulting cash surpluses and deficits?

4. What are the sources of cash (that is, borrowing) and under what conditions or in what context are they available?

Timely and rewarding short-term outlets will have to be found for the surpluses and appropriate outside financing arrangements will have to be made for meeting the deficit, so that operations continue unhindered and planned profits are realised. Does it then mean that these situations have only external remedies? Not necessarily. The cash planning goals can be communicated to the operating executives and their cooperation enlisted for realising these goals, without restoring to external assistance. The sales division can be requested to make special efforts to push up sales required to generate the necessary cash. Once this sales plan is pre-set and agreed to, the sales personnel can be relied upon to carry it out. The collection schedules can be reviewed and recast to yield the cash resources at the time needed. The purchase division can, if given information on the cash plan, rearrange its purchase schedules so as to
release cash for other pressing needs at specified points of time. It is thus evident that if the advance signals thrown up by cash planning are acted upon constructively, a major part of the problems of cash surpluses and deficit can be resolved by suitable and marginal readjustments in internal operations, without affecting the short-run profit goals.

Planning of the sources of cash will revolve mainly around sales. If all sales were for cash, the sales estimates themselves serve as estimates of cash inflows. But when cash and credit sales coexist, projection of cash realisations from sales and debtors assumes complexity. The sales personnel can competently aid in this planning exercise, equipped as they are with a first hand insight into the sales and collection patterns. The Finance Manager can, however, exhort them to improve over past experience by planning a higher proportion of cash sales to total sales or speedier collection of outstandings or other measures. Cash discounts can be planned as incentives for prompt settlement of bills, in periods when cash inflows have to be stimulated to forestall impending cash shortage. Odd transactions like sale of disposable assets can be suitably timed to generate cash at a time when it is needed. If the company has an adequate holding of liquid assets, especially short-term securities, planning for cash from operations does not have to be disturbingly intense. A credit line with a commercial bank
is another major safeguard against temporary cash shortages. But the establishment of such an external facility should not develop as a deterrent to cash planning. It is an expensive and not always dependable source, to be drawn upon only in emergencies, and so the cash planning drill has to be directed effectively to generate optimum internal resources from operations.

The uses of cash also need to be carefully planned. Payments to employees, inventory payments and payments for varied services, have to be examined and forecast. Questions such as taking advantage of cash discounts offered by suppliers need close attention to assess and effect the available cash savings. Besides planning the payment of various categories of operating expenses, the payments of taxes and dividends and the timings thereof have to be pre-planned. The repayment of loans, in accordance with agreed schedules, has to be provided for.

Planning Cash Balance:

It is essential that a certain minimum cash balance is over kept ready for emergency use. The quantum to be thus held may vary from company to company, and from time to time. This reservoir of cash balance acts as a levelling factor. It can receive temporary excesses in cash outflow. This reservoir cannot be allowed to go dry, as in that event, there can develop
a liquidity crisis and threat of insolvency. Nor can this reservoir be allowed to fill to the brim, because it will be expensive to hold large dose of idle cash and the return on investment will shrink. Thus arises the question; how much is too much? The answer will depend upon individual business situations. The level of production, pattern of demand, credit terms for purposes and sales, sources and prompt availability of credit, pattern of operating expenses etc. are factors that vary from industry to industry and company to company. The levels of adequacy of cash also vary correspondingly.

If excess cash is indicated in the cash plan, decision has to be taken on appropriate utilisation by making short-term investments, allowing some build-up in inventories, liberising credit, acquiring some fixed assets or repaying liabilities, even ahead of schedule. If cash shortages are expected, action called for may cover sale of some short-term investments, increasing the proportion of cash sales to total sales, aggressive collection of out standings, sale of some inventories (though at compromised prices), sale of disposable fixed assets and, as a final resort, borrowing funds from outside.
MANAGEMENT OF MARKETABLE SECURITIES:

Firms sometimes report sizable amounts of short-term marketable securities among their current assets. Why marketable securities be held? The two primary reasons as a substitute for cash and as a temporary investment:

As a Substitute for Cash:— Some firms hold portfolios of marketable securities in lieu of larger cash balances, liquidating part of the portfolio to increase the cash account when cash outflows exceed inflows. Data are not available to indicate the extent of this practice, but our impression is that it is not common. Most firms prefer to let their banks maintain such liquid reserves, with the firms themselves borrowing to meet temporary cash shortages.

As a Temporary Investment:— In addition to using them as a buffer against cash shortages, firms also hold marketable securities on a strictly temporary basis. Firms engaged in seasonal operations, for example, frequently have surplus cash flows during part of the year, deficit cash flows during other months. Such firms may purchase marketable securities during their surplus periods, then liquidate these securities when cash deficits occur. Other firms, particularly in capital goods industries where fluctuations are violent, attempt to accumulate cash or near-cash securities during a downturn in order to be ready to finance
an upturn in business volume.

Firms also accumulate liquid assets to meet predictable financial requirements. For example, if a major modernization programme is planned for the near future, or if a bond issue is about to mature, the marketable securities portfolio may be increased to provide the required funds. Also, marketable securities holdings are frequently large just prior to quarterly tax payment dates.

Firms may also accumulate resources as a protection against a number of contingencies. When they make uninsurable product warranties, companies must be ready to meet any claims that may arise. Firms in highly competitive industries must have resources to carry them through substantial shifts in the market structure. A firm in an industry in which new markets are emerging for example, foreign markets—needs to have resources to meet developments; these funds may be on hand for fairly long periods.
MANAGEMENT OF ACCOUNTS RECEIVABLE: CREDIT POLICY

The level of accounts receivable is determined by two factors:

1. the volume of credit sales and
2. the average periods between sales and collections.

The average collection period is partially dependent upon economic conditions during a recession or a period of extremely tight money, customers may be forced to delay payment - but it is also dependent upon a set of controllable factors, or credit policy variables. The major policy variables include (1) credit standards, or the maximum riskiness of acceptable credit accounts, (2) the credit period or the length of time for which credit is granted; (3) discounts given for early payment and (4) the firm's collection policy. We first discuss each policy variable separately and in qualitative rather than quantitative terms, then we illustrate the interaction of these elements and discuss the actual establishment of a firm's credit policy.

Credit Standards:

If a firm makes credit sales to only the strongest of customers, it will never experience bad debt losses, and it need not incur much in the way of expenses for a credit
department. On the other hand, it will probably be losing sales, and the profit foregone on these lost sales could be far larger than the costs it has avoided. Determining the optimal credit standard involves equating the marginal costs of credit to the marginal profits on the increased sales.

Marginal costs include production and selling costs, but we may abstract from these at this point and consider only those costs associated with the "quality" of the marginal accounts, or credit quality costs. These costs include (1) default, or bad debt losses; (2) higher investigation and collection costs; and (3) if less credit-worthy customers delay payment longer than stronger customers, higher costs of capital tied up in receivables.

Since credit costs and credit quality are correlated, it is important to be able to judge the quality of an Account. First, how should we define "quality"? Perhaps the best way is in terms of the probability of default. These probability estimates are, for the most part, subjective estimates, but credit rating is a well-established practice, and a good credit manager can make reasonably accurate judgements of the probability of default by different classes of customers.

To evaluate the credit risk, managers consider the five C's of credit, character, capacity, capital, collateral,
conditions. Character refers to the probability that a customer will try to honour his obligations. This factor is of considerable importance, because every credit transaction implies a promise to pay. Will the creditor make an honest effort to pay his debts, or is he likely to try to get away with something? Experienced credit men frequently insist that the moral factor is the most important issue in a credit evaluation.

Capacity is a subjective judgement of the ability of the customer. This is gauged by his past record, supplemented by physical observation of the customer's plant or store and business methods. Capital is measured by the general financial position of the firm as indicated by a financial ratio analysis, with special emphasis on the tangible net worth of the enterprise. Collateral is represented by assets that the customer may offer as a pledge for security of the credit extended to him. Finally, conditions refer to the impact of general economy that may affect the customer's ability to meet his obligations.

The five C's of credit represent the factors by which the credit risk is judged. Information on these items is obtained from the firm's previous experience with the customer, supplemented by a well-developed system of information-gathering groups. Two major sources of external information
are available. This first is the work of the credit associations. By periodic meeting of local groups and by correspondence, information on experience with creditors is exchanged. More formally, credit interchange, a system developed by the National Association of Credit Management for assembling and distributing information of debtor's past performance, is provided. The interchange reports show the paying record of the debtor, industries from which he is buying, and the trading areas in which his purchases are being made.

The second source of external information is the work of the credit-reporting agencies, the best known of which is Dun & Bradstreet. Agencies that specialize in coverage of a limited number of industries also provide information. Representative of these are the National Credit Office and the Lyon Furniture Mercantile Agency. These agencies provide factual data the credit manager can use in his credit analysis, and the agencies also provide ratings similar to those available on corporate bonds.

An individual firm can translate its credit information into risk classes, grouped according to the probability of loss associated with sales to a customer. The combination of rating and supplementary information might lead to the following groupings of loss experience.
<table>
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<th>Risk number class</th>
<th>Loss ratio (in percentages)</th>
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<tr>
<td>1</td>
<td>None</td>
</tr>
<tr>
<td>2</td>
<td>0 - $\frac{1}{2}$</td>
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<tr>
<td>3</td>
<td>$\frac{1}{2}$ - 1</td>
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If the selling firm has a 20 percent margin over the sum of direct operating cost and all delivery and selling costs, and if it is producing at less than full capacity, it may adopt the following credit policies. It may sell on customary credit terms to groups 1 to 5; sell to groups 6 and 7 under more stringent credit terms, such as cash on delivery; and require advance payments from group 8. As long as the bad debt loss ratios are less than 20 percent, the additional sales are contributing something to overhead.

Statistical techniques, especially regression analysis and discriminant analysis, have been used with some success in judging credit worthiness. These methods work best when individual credits are relatively small and a large number of borrowers are involved. Thus, they have worked best in retail
credit, consumer loans, mortgage lending, and the like. As the increase in credit cards and similar procedures builds up, as computers are used more frequently, and as credit records on individuals and small firms are developed, statistical techniques promise to become much more important than they are today.

Terms of Credit:

The terms of credit specify the period for which credit is extended and the discount, if any given for early payment. For example, if a firm's credit terms, to all approved customers, are stated as "2/10, net, 30", this means that a 2 percent discount from the stated sales price is granted if payment is made within 10 days, and the entire amount is due 30 days from the invoice date if the discount is not taken. Terms of "net 60" indicate that no discount is offered and the bill is due and payable 60 days after the invoice date.

If sales are seasonal, a firm may use seasonal datings. Jensen, Inc., a bathing suit manufacturer, sells on terms of "2/10, net 30 May 1 dating". This means that the effective invoice date is May 1, so the discount may be taken until May 10, or the full amount paid on May 30, regardless of when the sale was made. Jensen produces output throughout the year, but retail sales of bathings suits are concentrated
in the spring and early summer. Because of its practice of offering seasonal datings, Jensen induces some customers to stock up early, saving Jensen storage costs and also "nailing down sales".

The Credit Period Lengthening the credit period stimulates sales, but there is a cost to trying up funds in receivables. For example, if a firm changes its terms from net 30 to net 60, the average receivables for the year might rise from $100,000 to $300,000 with the increase caused partly by the longer credit terms and partly by the larger volume of sales. If the cost of capital needed to finance the investment in receivables is 80 percent, then the marginal cost of lengthening the credit period is $16,000 ( = $200,000 X 8 percent). If the incremental profit - sales price minus all production, selling, and credit costs associated with the additional sales-exceeds $16,000, then the change in credit policy is profitable. Determining the optimal credit period involves locating that period where marginal profits on increased sales are exactly offset by the costs of carrying the higher amount of accounts receivable.

Cash Discounts: The effect of giving cash discounts may be given an analysis similar to the one used for the credit period. For example, if a firm changes its terms from "net 30" to "2/10, net 30", it may well attract customers who want to take discounts, thereby increasing gross sales. Also, the
average collection period will fall, as some old customers will pay more promptly to take advantage of the discounts. Offsetting these benefits is the cost of the discount, taken. The optimal discount is established at the point where costs and benefits are exactly offsetting.

Collection Policy: Collection policy refers to the procedures the firm follows to obtain payment of past-due accounts. For example, a letter may be sent out when the account is 10 days past due; more severe letter, followed by a telephone call, may be used if payment is not received within 30 days; and the account may be turned over to a collection agency after 90 days.

The collection process can be expensive in terms of both out-of-pocket expenditures and lost goodwill, but at least some firmness is needed to prevent an undue lengthening in the collection period and to minimize outright losses. Again, a balance must be struck between the costs and benefits of different types of collection policies.

Accounts Receivable Versus Accounts Payable: Whenever goods are sold on credit, two accounts are created—an asset item entitled an account receivable appears on the books of the selling firm, and a liability item called an account payable appears on the books of the purchaser. At this point, we are analyzing the transaction from the viewpoint of the seller, so we have concentrated on the types of variable under his control. Later, in Chapter
FINANCING OF WORKING CAPITAL

There are two major sources short term and long term through which the firm's current assets are financed. Trade credit and cash credit (short term commercial bank loans) are the two primary sources of financing working capital in India. For every item of working capital, a specific source is suitable. Current assets or variable or temporary working capital should be financed by short term credit. Those assets which are less liquid should be financed from long term funds. John, J. Hampton has given three guidelines for financing working capital:

1. Guidelines 1: Permanent and variable working capital. The sources of funds are compared against the firm's permanent and temporary working capital. The remainders of the permanent working capital plus all the fixed assets should be financed from long term sources.

2. Guidelines 2: Major current - Asset Accounts cash and receivable are the most liquid assets and are or will soon be available to pay bills. There may be matched against current liabilities.

Guidelines 3: Total current Assets. A 2/1 normal current ratio means that one half the current Assets will be matched
against short-term liabilities. The remaining current assets and all fixed assets will be financed by long term sources of funds.

Advantages of long & short term sources of working capital are i.e.:

1. Lower Costs; 2. Establishers close relations with banks, (i) Reduces Risk, (ii) Provides stability and (iii) Increases Liquidity. Bank loans and trade credit together finance about 3/4 of the working capital requirements of industry. The banker, after scrutiny on the lines suggested by the Reserve Bank of India determines the maximum line of credit permissible for the period based on the margin requirements of the security offered. The margin is the percentage of the value of property offered as security by the firm which has to be financed by the firm itself. For example, if the banker insists on a margin of 30% on a particular item of inventory worth Rs.1,00,00, it means the banker will finance it upto Rs.70,000 (70%) and the balance of Rs.30,000 will have to be provided by the firm. The margin is based on the nature of the goods.

After getting the overall credit limit sanctioned by the banker, the company actually draws the fund needed from time to time (subject to the margin stipulation) using any or all the following forms of credit:
A. Loan Arrangement: Under this arrangement the entire amount of loan is credited by the banker to the party's account. Interest is payable on the entire amount, or when loan is repaid in instalments on the actual balances outstanding.

B. Overdraft Arrangement: Under the arrangement the party is permitted to overdraw on his current account with his banker upto a stipulated limit. There are no restrictions on the number of drawings within that limit. Repayments are permitted as and when desired during the period. Interest is charged on the amount actually utilized. These facilities are not available in a loan arrangement.

C. Cash Credit Arrangement: It is operated in the same way as a current account in which an overdraft has been sanctioned. The company may operate his account as and when required within the stipulated limit and can save interest by reducing the debit balance. However he has to pay a commitment charge of 1% on the balance unutilized during the period. Cash credit is usually allowed against pledge or hypothecation of goods and the borrower can provide alternative securities from time to time in conformity with the terms of advance.

D. Term Loans for WC: Under this arrangement the borrower can obtain a loan for a period of 3 to 7 years and repay the amount in yearly or half yearly instalments.
E. Bill Purchases and Bills Discounted: Sight bills, clean or documentary are purchased by bankers and usance bills are discounted. Whether bills are purchased or discounted, the amount made available under this arrangement is covered by the cash credit and overdraft limits. Before buying or discounting the bills the banker satisfies himself as to the credit worthiness of the drawer and the genuineness of bills.

Commercial establishment now a days working with borrowed capital. Borrowing is mainly from commercial banks for working capital at a cost of 18% rate of interest per annum. The profit generated during a year is ploughed back in the business and rarely it is used either for repayment or lowering down of working capital loans or other loans.

F. Export Finance: The exporter can apply to his banker "packing credit" which is short term advance granted by banks to exporters for assisting the exporters in buying, processing, packing and shipping the goods. The period of packing credit is normally 90 days. In special cases it is extended upto 240 days. A concessional rate of interest of 8% is charged on such advances. Any advance granted under this facility is to be liquidated by negotiation or purchase of the export bill covering the particular shipment for which the packing credit has been granted. If the export bill is drawn in a foreign currency, the exporter is require to sell forward
the foreign exchange to the bank so as to avoid risks involved in a possible change in foreign exchange rate.

In obtaining the commercial bank credit, the various modes security used are:

1. **Hypothecation**: It is mortgage of movable property. Under hypothecation, money is borrowed by the owner of goods on the security of movable property (usually inventories) without parting with the possession of movable property. The rights of the hypothecatee depend upon the terms of the contract between the parties. He can always file a suit to realise his dues by sale of the goods hypothecated. Creditor can not have prefential claim in the event of insolvency of the Borrower. Although advances against hypothecation of goods are riskier than advance against pledge of goods, the possibility of losses through dishonesty of borrower is very small.

2. **Pledge**: It is a kind of bailment by which one person transfers possession of some article to another for securing the payment of debt. The bailer is called "pawnor" and the bailee the "pawnee". Deposit of goods as security for a loan is essential. No pledge is created if there is no transfer or possession of goods. The pawnee is required to take reasonable care of goods pledged with him. He must not use the goods pledged and would be responsible for any loss or damage, if he does use them. The pledge lien
gives the pledgee the right to sell the goods in the event of the non-payment of the debt. The letter of pledge specifies the terms and conditions on which an advance is made, it is in the nature of a special agreement and modifies the rights the pledger has under the law to the extent required by the bank. Most of the clauses in the letter of pledge are incorporated as a result of practical difficulties experienced by banks from time to time.

3. **Lien**: It is the right of retaining goods belonging to another until a debt due to him is paid. Possessory lien is of two kinds: particular and general. Particular lien is a right to retain goods until a claim pertaining to those is paid. General lien can be applied until all claims of the possession are satisfied. Bankers enjoy general lien.

4. **Mortgage**: It is the transfer of interest in specific immovable property for securing the payment of money advanced. The mortgager parts with an interest in that property in favour of the mortgagee. Mortgage is not a mere contract, it is the conveyance of interest in the mortgaged property. The mortgagee's interest in the mortgaged property is terminated as soon as the debt is paid. The mortgager has the right to redeem or regain the property after pay off the debt.

5. **Charge**: Where immovable property of one person is by the act of parties or by operation of law made security for
payment of money to another, and the transaction does not amount to mortgage, the latter person is said to have a charge on the property and all the provisions applicable to simple mortgage will apply to such a charge.

That is:

(a) a charge is not the transfer of interest in the property though it is security for payment. But a mortgage is a transfer of interest in the property,

(b) a charge may be created by act of parties or by operation of law. But a mortgage can be created only by the act of parties,

(c) a charge need not be made in writing, but a mortgage deed must be attested,

(d) generally, a charge cannot be enforced against a transferee for consideration without notice. But in a mortgage the transferee of the mortgaged property can acquire the remaining interest in the property, if any left.

Long-term Capital:

We can make arrangements for the long-term capital required by an industry with the following:

1. Issue of right shares
2. Issue of preference shares
3. Issue of debentures.
Internal Sources of Funds:

There are some internal sources to meet out the demands of funds required for day-to-day operations. There are the following sources:

1. Retained earnings
2. Depreciation
3. Sales-tax collected but did not pay to the Government.
   This fund we can keep for two to three months till submission of returns.
4. Employee's deposits.
STUDY OF ABC RUBBER COMPANY LIMITED

MANAGEMENT OF CASH

EXISTING SYSTEM OF CASH FLOW:

Proforma of Cash flow has been attached in Annexure

SALES REALISATION - SOURCES OF INFORMATION:

All Divisional Managers Sales are asked to give the sales and collection of money during the month. They are also asked to give the outstanding receivables at the opening of month and at the end of the month. They provide these figures on the basis of goods allocated to their Division by the Coordination Manager Sales which takes the decision in the Sales Meeting which is held every month to review the Sales position.

DRAWBACK:

Divisional Managers are asked to give these figures on the first day of every month. Upto that date they did not know the position of goods allocation to their respective Divisions. So they give these figures on their own estimates which some times have variance from actual sales. Even the figures of outstanding receivables are generally not correct because Divisional Managers can not get the actual figures from their depots upto that date because depots are situated at distance places. So we see these figures can not be taken
as very reliable. A small variance can cause the disruption of payment programme.

SUGGESTIONS:

My suggestions to this situation is that sales meeting should be held by 11th day of each month and Divisional Managers should be asked to give the sales and collection forecast by 4th day of every month. By this date they can also collect the figures of actual outstanding receivables from their various depots. This will give authentic estimates and there will not be much variances. Cash flow can be prepared from 5th of every month of 4th of next month, this will give us more accurate picture of our sales collection and seeing the outstanding figures we can also plan the credit sales and cash sale policies.

PAYMENTS:

1. EXCISE DUTY: This payment can not be postponed or altered. If we have to sell our goods we will have to give the excise duty. If it deposited well in advance in the Government Accounts. So Excise Duty payments are made on Top Priority basis.

    There is no drawback in this system. According to daily despatches programme excise duty is deposited in the Bank.
2. **RAW MATERIALS:** In the Rubber Industry raw materials are very costly. In a company which produces 4,00,000 tyres, tubes and flaps annually about Rs.3,00,000/= worth of raw material is required for every month. This is a big amount. Some materials are of vital nature and cannot be procured immediately. Some imported raw materials take 4 to 6 months in procurement. They have to be planned well in advance and their payments cannot be postponed.

Suppliers send their bills to the costing department which after passing them send to the Head Office account, where they are immediately paid to the suppliers. For cash flow purpose an payment programme is given by the Purchase Manager to the Accounts department.

**DRAW-BACKS:**

Payments are immediately made by head office as soon as they receive the credit vouchers from the costing department. Credit facilities are not availed generally from the creditors. Some material can be procured within 3-4 days because of local availability of the material. Payment is made by draft.

**SUGGESTIONS:**

Every supplier must give some credit facility to accommodate the company. Payment must be made after the
expiry of credit period. Payment must be made by local cheques only so that some interest can be saved in the bank on account of cheques issued but not presented for payment.

Purchase department prepares the payment programme on the basis of supplies made by the suppliers. Some payments can be postponed for subsequent periods and only most important payments should be made in Company has some financial difficulty.

POWER AND FUEL:

These figures are supplied by factory people. These are mainly based on the running schedule of the plant. We found these figures completely authenticated. There is no need of any alteration in this. These payments can not be avoided or postponed as these things affect the production.

SALARIES AND WAGES:

These figures are taken on the actual basis. Generally these are only permanent staff and every month same amount is paid as wages and sales.

These payments can not be postponed and being made in the first week of every month.

In the existing system of company we find that salaries to all staff are being paid in cash. Our suggestion is that
Dated 12th April 1982

The Assistant Registrar, (Examinations),
Aligarh Muslim University,
Aligarh (U.P.)

Dear Sir,

I am sending herewith two dissertations duly examined by me as per V.P.P. as provided for in your rules. The amount of V.P.P. is accounted for as under:

1. Registered letter containing award list 3 = 35
2. " " to Asstt. Registrar 3 = 20
3. V.P. Parcel containing dissertations 13 = 25

Total postal charges 19 = 80

Thanking you,

Yours truly,

(Dr. R.B. Upadhyaya)

Encl.: Two postal receipts.
salary of the persons who are getting more than ₹.1000/= as salary should be given payment only by accounts payee cheque. By using this way company can also save some interest amount as these cheques will be presented for payment only after one or two days.

**CONSUMABLE STORES:**

These figures are supplied by commercial Manager who is the incharge of stores. They have a very good store purchase storage and store accounting system. Every month about ₹.8 lakhs worth of stores are consumed. For imported items they plan well in advance. Some materials are also being procured from local market. They have computerized control on store accounting. We do not see any fault in their existing system.

**INSURANCE:**

How much amount is to be paid to the Insurance Companies for the insurance of factory building, machinery and stocks of finished goods and raw materials, these figures are given by the Insurance Department which has experienced personnels. These figures are counter checked by the Accounts Department.

These payments are made on their due dates and can not be avoided for more than a week's time because there is always a risk of fire etc. We find these figures completely authenticated.
ADMINISTRATIVE MANUFACTURING & SELLING EXPENSES:

These figures are given by the factory accounts department and as well as by various departments of the head office. These figures are based according to the policies of the management. Generally budgets are fixed by the Management.

DRAW BACKS:

We have finding in this head there is not much control on expenses. Some departments incur heavy expenditure as Conveyance, Travelling and Staff Welfare expenses. There is no special checking on these expenses. Management never sees what is being spent on these heads except on several occasions.

SUGGESTIONS:

My suggestions in this area is that Management should have more control on these expenses. Every month about Rs. 32 lakhs are spent under this head. There are so many areas where expenses can be curtailed. If even one lac rupees can be saved in a month this will be a big achievement. Advertisement expenses can also be decreased if our sales are very high and we have lion's share in the market. Unnecessary telephone expenses can also be avoided by using call registers.
DEPOT'S EXPENSES:

Every month about Rs. 15 lacs are being spent for running the various depots which are situated in the major cities of India. These figures are supplied by the various Divisional Managers.

DRAW-BACK:

Head office has not a good control on Depot expenses. The major draw-back is that depot accounts are being audited by local auditors and management can not know the actual expenses incurred by the depots. Although Head Office receives expenses reports and statements from the depots every month but there is no authenticity in the figures of some items. Like on Loading and Unloading a huge amount is charged every month which does not provide proper receipts etc.

SUGGESTIONS:

My suggestions in this area is that Head Office after closely checking the requirements of the depots, should fix-up the targets for the expenses of these depots and only Budgeted amounts should be sent to depots for expenses. If they require some additional funds for any specific purposes they can be sent after the approval of the Management. Our second suggestion in this area is that some senior officers
of the company should visit the depots without informing them prior of the visit and he can checkup the various expenses incurred by them on the spot. If we could save only Rs. 50,000/= to Rs. 75,000/= per month in this head this will increase our profit and there will be more effective control on the depots.

**Interest:** This is the major expenditure head of the company. Being a Capital based project it had to borrow about Rs.16 crores from various Banks and financial institutions and about Rs.7 crores has been taken from various banks as working capital. Besides this, certain other loans have also been taken to meet the over run requirements. This has caused heavy payments of interest every month. These figures for cash flow purpose are supplied by Accounts department of site and Head Office.

**DRAW-BACK & SUGGESTIONS:**

There is no major draw-backs in the payment programmes. But it is suggested that some times if company is facing temporary financial crisis it should approach to the Financial Institution for the deferment of payment of interest. Under these circumstances, the financial institutions can give due consideration to the difficulties and allows the deferment without imposing any penalty or overdue interest. This can fulfil the gap temporarily working capital requirements.
And second suggestion is that company should try to repay the loans as early as possible by curtailing unnecessary capital expenses and various overheads to minimize the interest liability which in turn would result in increased profits.

**LOAN REPAYMENT:**

These figures are provided by Accounts Department. If we are short of funds we can ask the Banks and financial institutions for the deferment of these payments but if we are in a position to pay the loans we should affect these as this will save us from the high interest liabilities.

**SALES TAX:**

Every month about Rs. 80 lacs is collected by various depots under this head. Payment figures of Sales Tax are supplied by Taxation Department. These are based on the actual reports and statements of sales received by them from various Depots.

Sales tax collected provides the temporary working capital. Because in some states Sales Tax payments are made on monthly basis and in some states on quarterly basis so up to that time we can use that money as per our requirements. These payments can be postponed for some time if we are short of funds. Generally Sales Tax Officers accommodate in such situations.
ROYALTY: Payment of Royalty is made every Quarterly. On the sales of the company. There are various legal for this payment. This payment can be deferred for some time if we are short of funds. This is not such an urgent payment.

SECURITY REFUND: Every month some amount is refunded to various dealers as security refund. This constitute only about ₹. 50,000/= or ₹. 75,000/= in a month so there is no problem in paying this amount.

CAPITAL EXPENSES: Every month about ₹. 20 lacs is being spent on the purchase of various imported and indigenous machinery and spare parts and on building work. These payments represent the extension programme of the company. These are made on the availability of funds. Figures for these payments are supplied by Plant Manager.

FIXED DEPOSIT REFUND: Every month about ₹. 5 lac is being refunded to the Fixed Depositors. These payments can not be avoided and company makes them in time to earn the good name among investors.

GENERAL: Thus we see various payment figures are given by various department which are compiled by Accounts Section at Head Office and they write these figures in the column of payment asked for. In the first column figures given by Costing Department are written. These are based on the production programme. In the third column Expected Payments
are written. These are prepared by Accounts department subject to the availability of funds and as per Sales Realisation Programme. Surplus or Deficit figures are calculated and are being given in the cash flow statement.

SUGGESTIONS:

It is suggested new proforma for the cash flow which has been enclosed in this report as Annexure No. 2. In this proforma Receipts and Payments will be shown on weekly basis. By using this we would be able to know our weekly surplus of deficits and Payment programmes can be replanned according to the availability of the funds. We found that no comparative statement is being prepared by the company at the end of the month. We suggest that at the end of the month Actual Receipts and Payments should be compared with the given figures and reasons of variances should be seen closely so that next time there should not be any difference.
### ABC CO. LTD.

**CASH FLOW FOR THE MONTH OF .....**

(Rs. in lacs)

<table>
<thead>
<tr>
<th>As per production programme for current month</th>
<th>Payment asked for</th>
<th>Payment expected</th>
<th>Actual Exp. for last month</th>
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**EHS**

**AL PAYABLES**

plus (Deficit)

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qus issued but presented
# ABC CO. LTD.

CASH & BANK BALANCE REPORT AS ON.....

REPORT NO.......  

## CURRENT ACCOUNTS

<table>
<thead>
<tr>
<th>NAME OF BANK</th>
<th>OPENING BALANCE</th>
<th>RECEIPT/ INTER BANK TRANSFER</th>
<th>DISBURSEMENT</th>
<th>BALANCE</th>
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<tbody>
<tr>
<td>Punjab National Bank</td>
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<td>State Bank of India</td>
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<td>Allahabad Bank</td>
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<td>Syndicate Bank</td>
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<td>India Bank</td>
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<td>P &amp; S Bank Ltd.</td>
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<td>Cash in Hand</td>
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## CASH CREDIT ACCOUNTS

<table>
<thead>
<tr>
<th>NAME OF THE BANK</th>
<th>SANCTIONED LIMITS</th>
<th>AVAILED</th>
<th>BALANCE</th>
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<tbody>
<tr>
<td>State Bank of India, Bombay</td>
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<td>State Bank of India, New Delhi</td>
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<td>P.N. Bank, Bombay</td>
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<td>State Bank of Patialia</td>
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| Stock of Raw Material                     |                   |         |         |
| Stores, spares, and Goods in process and Govt. Book Debts. | ................. |         |         |

| Stock of Finished Goods.                   |                   |         |         |
| At plant ₹.......................... |                   |         |         |
| At Depots ₹.......................... |                   |         |         |

| **TOTAL**                                  |                   |         |         |
| Balance D.P. available ₹................... |                   |         |         |

Prepared by Accountant Controller of Accounts Finance Manager

* Cheques issued but not presented for payment ₹.
ABC CO. LTD.

ANNEXURE "B"

CASH FLOW FOR THE MONTH OF

<table>
<thead>
<tr>
<th>Payment asked for</th>
<th>Payment expected</th>
<th>1st Week 1-8</th>
<th>IIInd Week 9-16</th>
<th>IIIrd Week 17-23</th>
<th>IVth Week 24-31</th>
<th>Actual for last month</th>
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<tbody>
<tr>
<td>Payment asked for</td>
<td>Payment expected for</td>
<td>1st Week 1-8</td>
<td>IInd Week 9-16</td>
<td>IIIrd Week 17-23</td>
<td>IVth Week 24-31</td>
<td>Actual for last month</td>
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Surplus/deficit per week

Cumulative

Bank balance as on 1st of this month

Closing balance
ABC CO. LTD.

SALES REALISATION FOR THE MONTH OF

<table>
<thead>
<tr>
<th>U.P. Zone</th>
<th>1st Week</th>
<th>IInd Week</th>
<th>IIIrd Week</th>
<th>IV Week</th>
<th>Actual for last month</th>
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<td>North Zone</td>
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<td>Total</td>
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INTEREST PAYMENTS

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<tr>
<th>Total amount</th>
<th>1st Week</th>
<th>IInd Week</th>
<th>IIIrd Week</th>
<th>IVth Week</th>
<th>Actual for last month</th>
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<td>Terms LoansSBI</td>
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<td>Others</td>
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<td>Raw Mat.</td>
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<td>Promoters</td>
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<td>Others</td>
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<td>Total</td>
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ABC CO. LTD.

DAILY COLLECTION STATEMENT

Dated

<table>
<thead>
<tr>
<th>S1. Name of Depot</th>
<th>Collection to-day</th>
<th>Collection to-date of this month</th>
<th>Collection target to-date of this month</th>
<th>Collection to-date of previous month</th>
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<tbody>
<tr>
<td>Kanpur</td>
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<td>Lucknow</td>
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<td>Agra</td>
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<td>Direct Receipt at site and Head Office</td>
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<td>Bombay</td>
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<td>Export</td>
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<tr>
<td>Total Sales</td>
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<tr>
<td>Realisation</td>
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</tbody>
</table>

Prepared Accountant COA Finance Manager

CC : Vice Chairman, Executive Director, President, ACOA, UP Zone, North Zone, East Zone, South Zone, West Zone.
WORKING EXPENSES FOR THE MONTH OF

( Rs. in Lacs)

<table>
<thead>
<tr>
<th>Factory Head Office Total</th>
<th>Ist Week</th>
<th>II Ind Week</th>
<th>III Week</th>
<th>IV th Week</th>
<th>Actual for last month</th>
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<tbody>
<tr>
<td>A: Power &amp; fuel</td>
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<tr>
<td>Electricity charges</td>
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<tr>
<td>Coal &amp; its freight</td>
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<td>Sub Total</td>
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<tr>
<td>B: Salaries &amp; Wages</td>
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<tr>
<td>C: Consumable Stores</td>
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<tr>
<td>D: Insurance</td>
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<tr>
<td>E: Administration, Mfg. &amp; Seeling Expenses</td>
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<tr>
<td>Freight on Raw Material</td>
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<td>Freight on Sales</td>
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<td>Advertisement</td>
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<tr>
<td>Selling Expenses</td>
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<td>Repairs &amp; Maint.</td>
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<tr>
<td>Travelling Exp.</td>
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<tr>
<td>Staff Welfare Expenses</td>
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<td>Total Exp.</td>
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<td>P. &amp; T.</td>
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<td>TOTAL</td>
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</table>
## ABC CO. LTD.

### DISBURSEMENT & RECEIPT STATEMENT

**Dated...........**

<table>
<thead>
<tr>
<th>SL No.</th>
<th>PAYMENTS</th>
<th>TODAY</th>
<th>TODATE THIS MONTH</th>
<th>TARGET TO DATE OF THIS MONTH</th>
<th>TODATE OF PREVIOUS MONTH</th>
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</thead>
<tbody>
<tr>
<td>1.</td>
<td>Excise Duty</td>
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<tr>
<td>2.</td>
<td>Raw Material</td>
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<tr>
<td>3.</td>
<td>Working Expenses</td>
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<tr>
<td>4.</td>
<td>Depot Expenses</td>
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<td>5.</td>
<td>Sales Tax</td>
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<tr>
<td>6.</td>
<td>Income Tax</td>
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<tr>
<td>7.</td>
<td>Interest</td>
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<td>8.</td>
<td>Capital Expenses</td>
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<tr>
<td>9.</td>
<td>Loan Repayment</td>
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<td>10.</td>
<td>Royalty</td>
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<td>11.</td>
<td>Security Refunded</td>
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<td>12.</td>
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<td>14.</td>
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</table>

**TOTAL PAYMENTS**

**TOTAL RECEIPTS AS PER DETAILS ATTACHED**

Prepared by Accountant Controller of Accounts Finance Manager
MANAGEMENT OF INVENTORY:

Inventory is defined as goods in possession for resale. Inventories may be durable, or nondurable, perishable or non-perishable, valuable or inexpensive. Inventory policies have a direct and important bearing on the financial needs of the firm.

Inventory constitutes the major element in the working capital of any business undertaken. RBI made a study of 1650 companies in the year 1973-74 and have found that inventories constitute about 37% of the investment in current assets. The major portion of current assets is invested in inventories and, therefore, inventory management has a significant role in the working capital management.

In U.S. Income-tax data from the Internal Revenue service show that inventories average approximately 20% of a manufacturing firm's total assets. For retail firms, the figure is closer to 30 percent. Every industry either it is small or big has to keep inventories. The ideal method of working is not to have any inventory, but that is impossible. No trading or manufacturing business can be run without keeping any inventory. Inventory may be low or big but always remains there.
NEEDS TO HOLD INVENTORY:

1. To make availability of materials required for production for maintaining smooth flow of production operation.
2. To get benefit of low price or discount on bulk purchases.
3. To meet an ever increasing demand for prompt customers.
4. To keep hold on certain vital or critical supplies such as spares and tools without which production is stopped.
5. To minimise costs and maximise profits.
6. To promote flexibility in plant scheduling.
7. To maximise sales and take highest market share.
8. To manufacture goods in economic production runs.

The inventory policy of the company have a direct effect on the financial needs of the company. In view of changing inventory decisions and policies the funds position of the company will also undergo changes. It is, therefore, very essential to keep the inventory under constant review. To summarise the benefits to a firm are avoiding cost of sales, gaining quantity discounts reducing order costs:

Here are some objectives of controlling the inventory:

1. To control the capital investment.
2. To control the inventory carrying cost.
3. To control the re-ordering cost.

In a manufacturing concern there are generally four type of inventory:
1. Raw Materials
2. Goods in process or working process.
3. Finished goods
4. Stores and spares

RAW MATERIAL - MANAGEMENT:

Raw materials are those goods that have not yet been committed to production in a manufacturing firm. For each manufacturing concern raw materials are required. As production is nothing but a conversion of raw materials to finished goods with the help of certain processes. In inventory, raw materials play a vital role, as maximum cost of inventory is blocked in raw materials. For example, in Modi Rubber Limited, an automobile tyres and tubes manufacturing plant, stocks of raw materials both in stock and transit remains to the tune of about Rs. 4 crores against the total inventory of Rs. 10.5 crores. It means about 38% inventory is of raw materials only against the total inventory.

To keep proper control over the inventory of raw materials, it is very much essential that stock levels of raw materials should be kept as minimum as possible keeping in view the all aspects of continuous supply of raw materials, inventory carrying cost, re-ordering cost and stock-out cost. For example of a ABC Company Ltd. where material A which is the main raw material is used about 32 Tons per day carrying a cost of Rs. 2.5 lacs. The purchasing point of this raw
material is Cochin. The minimum stock level of this raw material is kept for 10 days stock in store and 17 days stock in transit. This level is fixed with a view that from Cochin to site, transit period by rail is about 15 days. There is a continuous supply of wagons from Cochin on production scheduling basis. This company in practical keeps the stocks of this particular item about 12 to 13 days which is also a maximum level fixed by the company. Some times, this maximum level is crossed due to the following two reasons:

1. Change in production programme
2. Some times, wagon despatched from Cochin does not reach site in time due to some unavoidable circumstances and to avoid any shortage of material fresh lot is sent in place of that consignment. Some, it has been experienced that both the consignments reach together with a gap of one or two days. In that case inventory goes high and is to be control by stopping that much quantity to despatch.

This company also tried to keep minimum stock of this item for eight days but that was not feasible as it has happened many a times particularly incase of railway strike that this material had to procure by road transport. The transit time by road is 7 to 8 days but in practical way, sometimes truck are held up and reach site in 9 to 10 days. Therefore, to avoid any stock-out position, this company has kept minimum stock level of this item for 10 days.
For fixing of stock level of raw material, many points are to be kept in view like :-

1. Source of supply
2. Either supplier is one or more suppliers
3. Production of that supplier in case of one supplier
4. Other users of that particulars raw material
5. Our share out of that production
6. Production scheduling of that supplier and our production scheduling
7. Transit time

For example, in ABC Company Ltd. raw material named 'B' is used about 8 Tonnes costing ₹.90,000/= per day. This raw material is supplied from such centre where transit time is less than one day. But you will be surprised to know that minimum stock level of this raw material is to be kept 30 days in store. Why it is so? Why inventory is held up for ₹.27 lacs which can be kept in ideal way 4 to 5 days i.e., for ₹.4.50,000/= the reason is:

1. Supplier is one
2. That particular type of material is produced by that supplier once or two times in a month.

Though the transit time is one day but we have to keep in every condition 30 days stock with a view that if that particular batch of material is manufactured only last
the month that can reach factory before stock-out position. Therefore though there are some specified system to keep minimum and maximum stock level, but in practical life, these are also viewed with the other prevailing factors like in case of 'B' category raw material of ABC Company Limited.

MANAGEMENT OF WORK-IN-PROCESS INVENTORY

The work-in-progress inventory or goods in process are those materials that have been committed to the manufacturing process but have not been completed. In other words goods are not yet ready to sale.

The work-in-process inventory in an industry is a function of the manufacturing technology, that is whether the industry is of a continuous process type or a batch production type. In the case of the continuous process the value of work-in-process inventory is generally fixed and depends on that particular process and/or the capacity of the machinery i.e., how much material is in the machine under the process stage. An example of this type of production might be nylon, fertilizers and oil refineries. On the other hand in firms which are employing 'batch process' type of production process the work-in-process inventory can vary significantly a discussion of three salient aspects of the 'batch process' work-in-process inventory management follows:-
Problem Definition/Choice of Decision Paths

Many industries have some technological characteristics which require that the processed material be used immediately or some aging process. The tire industry is one such industry. There is always a minimum time which any in-process material can be kept before the quality of the material deteriorates with the passage of time. In the typical case of the process for manufacturing tires the minimum and maximum time required for the mixed rubber compound are fixed. The minimum time is equal to the aging time which must be completed before the next process on the same material can take place. The maximum limit is the time before which it should be consumed in order to prevent over aging and deterioration in quality. In the case of the rubber industry, the minimum aging time is four hours and the maximum is 24 hours. Similarly, in the case of Alcoholic drinks manufacturing industry, it is seen that the quality of the Alcohol being produced improves with the passage of time. Whatever may be the situation it would depend upon the type of industry but it is clear that the management has a task before itself to see that the limits are maintained within minimum and maximum levels so that the ultimate objective of control over work-in-process inventory is achieved.
Problem Definition: General impression in the mind of people is that industry having minimum work-in-process inventory is most efficiently run undertaking. If sophisticated machines are being used then objective should be to optimise the following costs, as a unit, and not separately:

a) Machine setting up cost; and
b) Inventory carrying cost.

It will be seen if the number of set ups of a machine is increased then set-up cost will increase while inventory carrying cost will come down. On the other hand if the number of set-up is low then the setting up cost will be low but the Inventory Carrying Cost will increase. Therefore the objective should be to minimize the total cost which is the arithmetical sum of the two cost.

DATA:

Name of Machine = A
Product produced = X
Cost of setting up machine = ₹.500/= 
Number of X required/day = 200
Daily inventory carrying cost = ₹.0.50
Production requirement = 1000 pcs
ANALYSIS:

No. of set-ups = 1

Inventory at the end of first day = 800

Inventory at the end of second day = 600

Inventory at the end of third day = 400

Inventory at the end of fourth day = 200

Total cost (when number of set-ups is the minimum i.e., 1)

= Set up cost + Inventory carrying cost

= No. of set-ups x set-up cost + number of pieces x Daily inventory carrying cost

= 1 x 500 + 800 x 0.5 + 600 x 0.5 + 400 x 0.5 + 200 x 0.5

= 500 + 400 + 300 + 200 + 100 = Rs.1500

Total cost (when No. of settings is maximum i.e., 5)

= No. of setting x setting up cost + No. of pieces x Daily Inventory carrying cost

= 500 x 5 + 0 x 0.5 + 0 x 0.5 + 0 x 0.5 x 0 x 0.5

= Rs.2500

This point clarifies that the objective of the management should be to minimise the setting up cost as well as inventory carrying cost rather than only minimization of inventory management policies also have significant influence on the investment in working process inventory. From the abovementioned case, it is clear that the total cost in
setting up as well as inventory carrying cost is equal to Rs.1,500/= against the total setting up cost of Rs.2500/= if the machine is set up on daily basis. Therefore right alternative is that X should be produced and stored rather than setting up machine on daily basis.

It means that stock in work-in-process differs from company to company. It is more basically depends upon the process system. Moreover, efforts should be made to keep the inventory as minimum as possible keeping in view the all other factors like machine set-up cost etc. etc.

Inventory of work-in-process also goes high sometimes or becomes low sometimes due to production scheduling. Some-time actions that speed the production process may increase out put without proportionately increase in the work-in-process inventory. On the other hand the firms with not good production scheduling may face problems and delays and as a result find much larger amounts lied up in the work-in-process inventory.

MANAGEMENT OF FINISHED GOODS:–

Finished goods are those goods that have been completed and awaiting for sale. Inventory of finished goods plays a very vital role in the inventory management. Stocks of finished goods mean goods–awaiting for sale. They are the final output of the production process as for as a manufac-turing company is concern. In case of retail firms and
wholesalers, they are usually referred to as the merchandise inventory. The increase of inventory of finished goods means low sale. Therefore, basically it is the duty of the sales manager to see that inventory of finished goods should not be increased. They should promote sales to clear the inventory of finished goods. Since stock of finished goods contribute to a good percentage of total inventory cost it is also an important part of the inventory management. When stock of finished goods inventory increased, it exposes a number of risks and costs there should be a trade off between having too little and too high inventory. We have seen the risks and cost in achieving this trade off. Some costs have less risk as some other costs have higher risk. Our purpose should be to reduce risk, hold down costs and increase revenues. To keep the inventory carrying cost of finished goods as much as possible, two aspects come into play.

1. **Sales Aspect:** As inventory of finished goods increases due to less sales, so efforts are to be made to promote sales. Following points are to be observed for this:

   (a) Stop production in view of sluggish demand and already high inventory with the company.

   (b) Produce goods with expectation of sales in future.

   (c) Produce a product which may have lower profit margin but immediate sales prospects instead of an item which has higher profit margin but low sales prospects.
(d) To promote sales by giving discount to clear inventory keeping in view the inventory carrying cost. Discount should not increase that the inventory carrying cost.

(e) To change products, sizes, designs, quality etc.

(f) To change packing material to attract the market.

(g) To start a bonus scheme keeping in view the profit margin.

These above steps are taken by the inventory management with the help of production people and sales people. Actually, it is the duty of sales management and production management to keep a proper watch on the finished goods items. They should produce those things which are easily acceptable by the market. Marketing management also plays a vital role in this aspect.

FINISHED GOODS INVENTORY CARRYING COST:

Inventory carrying costs are the those expenses which are incurred in storing goods. Classifications of finished goods inventory cost will be done by way of capital tied up in the inventory at all stages. For example, in plant premises till such time as no excise has been levied the cost consists of only the fixed and variable cost elements, while in transit the cost consists of excise paid and the transit charges being incurred. At the depot the cost further goes up and includes the distribution expenses and other
indirect expenses as incurred in the godown. Finished goods inventory carrying cost has following kinds:

1. Storage Cost: Storage space as warehouse or supply room is needed to store the finished goods, to look after it workers are employed. Labour is employed to move, clean record and protect the goods.

2. Insurance: Insurance is necessary against hazards like fire or accident in warehouse. Insurance premium represent finished goods carrying cost on inventory.

3. Obsolescence and Spoilage: Obsolescence and spoilage are two different inventory carrying costs. Obsolescence is the cost of being unable to sell goods because of current market factors deriving from changes in style tastes, or other factors. Spoilage cost occurs when a product is not salable because of deterioration during storage, like foods that rot, plants that die.

4. Damage or Theft: In spite of all efforts there are chance of damage of goods and theft this loss will not be covered by insurance and becomes an item of inventory carrying cost. It is the job of the inventory control department that they should keep a vigilant watch on the stocks of transit and depots. Stocks in transit and depots should not go high as it includes the cost of excise, distribution expenses and other indirect expenses. Food back should be in such a way that depots should have minimum
CASE STUDY ON BUILDING THE FINISHED GOODS INVENTORY FOR FUTURE SALE:

Problem Definition: One of the basic objectives of controlling the finished goods inventory is to maximise the sales or market share in such a way so as to optimise the profits. Often the problem in a multi product company is to make a choice between the product which may have lower profitability but immediate sales prospects instead of one which has higher profitability but lower sales prospects.

IN ABC Company there are different type of products and their salability keeps on changing. The choice has to be made between making product 'A' or product 'B' or product 'C' or product 'D' depending upon the market condition.

Following data were collected to illustrate the problem as above.

PROBLEM DATA:

It was found that the company could produce 4000 'A' product with given production constraints in the same period the company could produce 3000 'B' product with no additional production cost from the point of view of production. Other relevant data is as below:
\[ c_{s1} = \text{Unit inventory carrying cost per day at 18\% cost of the capital on manufacturing cost of } ₹800=\text{ per product.} \]
\[ c_{d1} = \text{Cost of deterioration per product which is } ₹1=\text{ per product.} \]
\[ c_{1} = \text{Net profit which is } ₹50=\text{ per product.} \]

In case of product 'B':

\[ c_{s2} = \text{Unit inventory carrying cost per day at 18\% cost of the capital for the manufacturing cost of } ₹1050= \]
\[ c_{d2} = \text{Cost of deterioration per product which is } ₹2.5 \]
\[ c_{2} = \text{Net profit which is } ₹50=\text{ per product.} \]

The problem before the company is whether to produce 4000 A products which has possibilities of being sold after being retained in stock for 30 days. On the other hand, other is equal chance of selling 3000 B products after about 80 days. The problem which is being faced is whether to make and store 4000 A products or to make and store 3000 B products with the expectation of sales in the future as already outlined.

**CHOICE OF DECISION PATHS & A PRODUCT:**

\[ C_{s1} = 800 \times 0.05/100 = ₹.40 \text{ per day product} \]
\[ C_{d1} = ₹1= \text{ per product} \]
\[ C_{1} = ₹50= \text{ per product} \]
\[ n_{1} = 400 \text{ nos.} \]
\[ m_{1} = 30 \text{ days} \]
Therefore in case of the A product total profit contribution is:

\[ n_1 c_1 \]
\[ = 4000 \times 50 \]
\[ = \text{Rs. } 200,000 \]

The total cost of carrying the inventory and other relevant costs are as follows:

\[ c_{cl} n_1 m_1 + c_{dl} n_1 \]
\[ = .40 \times 4000 \times 30 + 1 \times 4000 \]
\[ = 48,000 + 4,000 = \text{Rs. } 52,000 \]

The net profit, therefore, in case of product 'A':-

\[ \text{Rs. } 2,00,000 - \text{Rs. } 52,000 = \text{Rs. } 148,000 \]

for product 'B':

\[ c_{22} \]
\[ = \text{Unit inventory carrying cost per day at 18% cost of capital of manufacturing cost of the product.} \]
\[ = 1050 \times \frac{.05}{1000} = \text{Rs. } .525 \text{ per day product} \]

\[ c_{d2} \]
\[ = \text{Cost of deterioration per product} \]
\[ = \text{Rs. } 2.5 \text{ per product} \]

\[ n_2 = 3000 \text{ nos.} \]
\[ m_2 = 80 \text{ days.} \]

Therefore in case of product 'B' the total contribution is:

\[ n_2 c_2 \]
\[ = 3000 \times 150 \]
\[ = \text{Rs. } 4,50,000 \]
The total cost of carrying inventory for this period and other relevant costs are:

\[ c_{s_2} n_2 m_2 + c_{d_2} n_2 \]

\[ = 0.525 \times 80 \times 3000 + 2.5 \times 3000 \]

\[ = 126000 + 7500 \]

\[ = \text{Rs. 1,33,500} \]

In case of product 'B' therefore:

\[ n_2 c_2 + c_{s_2} n_2 m_2 + c_{d_2} n_2 \]

and which gives the necessary as well as sufficient condition of:

\[ n_2 c_2 - (c_{s_2} n_2 m_2 + c_{d_2} n_2) \]

\[ = \text{Rs. 4,50,000} - \text{Rs. 1,33,500} \]

\[ = \text{Rs. 3,06,500} \]

It may be observed that necessary and sufficient conditions for making the product 'B' is as below:

\[ n_2 c_2 - (c_{s_2} n_2 m_2 + c_{d_2} n_2) \]

\[ p_1 n_1 c_1 - (c_{s_1} n_1 m_1 + c_{d_1} n_1) \]

The above condition is observed as:

\[ \text{Rs. 3,06,000} \quad \text{Rs. 1,48,000} \]

The company will stand to gain Rs. 1,58,500 by choosing the alternative of producing the product 'B'.
MANAGEMENT OF STORES AND SPARES INVENTORY CONTROL:

Apart from raw materials, a manufacturing firm has to carry inventory of stores and spares and purchased components etc. Many of the methods of stores and spares inventory control are similar to the raw material inventory control. Methods like Kardex system and Two Bin System are quite common and everyone in the industry is aware of these techniques. I feel no need to go in details for these systems.

In large size manufacturing firms the number of stores and spares can be anything from 15,000 to 30,000. Taking their inventory at the end of the financial year is impossible because of the huge work involved in counting each and every item or weighing each and every item.

Perpetual Inventory System:

Perpetual inventory system is a system by which one can keep track of inventory. This system is in addition to the system for establishing stock and reorder levels for individual items. In simple words a perpetual inventory system is a continuous stock taking system spread over a period. The important items may be subjected to more frequent and larger number of varifications during the year. The main advantage of this technique is that plant operation does not disturb while taking the stocks/inventory.
Items that are to be verified can be selected at random, such that the items chosen for surprise check are as near to minimum levels as possible, as per stock records or bin cards. The verification is easily done in this instance unlike the annual inventory where huge inventories of some items might pose serious counting or weighing problems. With the amount of the work reduced, a larger number of items of inventories can be certified each day than would otherwise be possible. If on verifying the count of the selected items shortages are spotted, the situation may call for immediate action to replenish stocks. Thus, the perpetual inventory system provides verifications of the information furnished by the bin cards and enables correction of recording errors rendering them reliable as basis for inventory decisions.

Perpetual inventory system compiles prompt updating of stock records on a continuous basis. The personnel who are assigned the task of physical verification of stocks under perpetual inventory system are experienced and familiar with the items, and can identify them properly. In annual stock taking, many employees who are unfamiliar with the items may be engaged to verify the inventories and the possibilities of wrong identification and counting errors are higher. Moreover, perpetual inventory helps prompt detection of discrepancies facilitating speedy investigation.
John J. Hampton has given the following figure for need of inventory:

- Avoid losses of sales
- Gain quantity discounts
- Reduce order costs
- Achieve efficient production

Why Firms Hold Inventory: Separate inventories to:

- Purchasing
- Producing
- Selling
Annual stock taking highlights the discrepancies long after the occurrence, in most cases, and is less effective.

**CASE STUDY:**

In ABC Company limited there are total 13000 items out of which 8000 items are stock items. These are those items which are either insurance spares or consumed regularly or consumed by more than two users. Items of capital nature, obsolete nature, very rarely required or raw materials are not included in stock items.

To keep proper control over these 8000 items, the following steps are taken:

(a) There is a bin card system in the factory under the store department for proper recording of the documents.

(b) Perpetual inventory system: There is perpetual inventory system in the factory. For this job, a separate cell has been set up under Accounts department. This cell takes physical stock of all the items in such manner that consumables are counted at list twice a year and insurance spares once a year. They also check bin card stock against ledger stock taking at the time of finalisation of balance sheet.

To keep proper control over inventory the following procedures are also adopted in a ABC Company Limited.
1. CODIFICATION

Since number of items in ABC Company are very large and also for easy identification of individual item for detailed specification, a coding scheme has been introduced whereby each individual item is given a separate code and a standard unit of measurement. After giving code number it becomes very easy to control every item separately. As it helps in counting etc.

Code is of seven digits. Each digit indicates some specification of the material. Given below significance of each individual digit:

/ / 

All the items are divided into two main Groups:

A. General Items
B. Spare Parts

GENERAL ITEMS: 1st digit of item code means; main group
1Ind & 3rd digit of item code means; sub-group
4th-7th digits of item; Flexible digits

SPARE PARTS:
1st digit is common, specifying that item is spare
2nd to 4th : Equipment
5th to 7th : Flexible digits
INDENT VERIFICATION

Material is purchased by the Purchase Department only against specific indent, which is raised either by stock Control Section, for items which have been declared stock card items under authority of Plant Manager or by the individual User Department.

Such idents are authorised by the Departmental Heads only. For items of personal use, furniture, capital item and costly items idents are put up to the Management for sanction.

All idents other than stock card items are sent to the Issue Store for verification of stock in hand.

Issue Store indicate the stock availability against individual item on indent and send the same, after giving a running serial no., to Purchase.

Purchase procures only such material which is not available in Store.

Issue Store also suggest use of alternate material, if available in the Issue Stores, for keeping the inventory to the minimum extent.

ABC ANALYSIS:

Since hold of inventory means hold of finance. So every item of inventory is valued in rupees. Basically, it has been observed that there are three types of items in every manufacturing unit. Some are those items which are
of high value. Some are those items which are to medium value. Some items are those which have minimum value. To segregate these items ABC analysis system has been introduced. In this system, an analysis of items and their value is made in order to show how inventory value is concentrated amongst the individual items. This analysis is made by classifying the items in three categories i.e., A, B and C. Classification is based on value, usage rates and criticality. The items are taken by their value and then the accumulated percentage of each item is related to the total value of all inventories. Generally the analysis comes:

1. 10% of items hold 70% of the value
2. 20% of items hold 20% of the value
3. 10% of items hold 10% of the value

CASE STUDY:

A thorough study of ABC analysis system introduced in A.B.C. Company was made and found that

1. 6% of items hold 80% of the value
2. 10% of items hold 10% of the value
3. 84% of items hold 10% of the value

From the above statement it will be realised that 6% of items are carrying 80% of the value so management should pay more attention for controlling 6% items instead of wasting time
in 82% of items which carry only 10% of the value. Key items are the 6% attention should be given to their attention paid in controlling the 6% of items may decrease the inventory cost of the factory. The 6% of the items are high value items and are to be considered in A category, 10% of the items are medium value item and are to be considered in B category and -82% of the items are having low value and considered in C category. So different control mechanisms have to be devised for each category. For the best control and to reduce the cost more care and attention should be paid to A category that are 6% of the items category. And less attention should be paid to C category that are 83% of the items with 10% of the value.

APPLICATION OF STANDARDISATION:

When we go for codification, we group all the like items together which makes it easy to examine the complete range of any given type of stores and consider whether the number of varities can be reduced. In every factory, there are some items which are very similar in function, but points are to be seen whether it is economically possible to fix a standard of various varities. For example, in a factory where different types of electric bulbs are required like 60 watts, 40 watts and 25 watts it is to be seen whether it is economically feasible to keep only 40 watts
bulbs or 25 watts bulbs instead of keeping all the three items. This can be visualised with the help of consumption value and functional value. In case with the help of standardisation, we reduce the variety we can get price discount in purchasing bulb quantity.
PROCEDURE FOR RECEIPTS AND ISSUE OF MATERIAL: ACCOUNTING:

Any purchase results from demand created by the production or other using departments in the factory. In case of raw materials, to achieve a particular level of production, the material breakdown is provided by the Chief Chemist (Production Planning Department). With this information, the Purchase Department recommends the approved levels of inventory, giving due consideration to location of suppliers, value of the material involved, the availability of raw materials etc. The Purchase Department obtains approval from the Management for (A) level of inventory to be maintained in the plant (expressed in month's requirements), (B) quantity that should always be in transit (expressed in month's requirements), and (C) quantity that should be 'on order' with the suppliers (expressed in months' requirements). The approval is on the basis of stocks for each class rather than for each raw material. Purchase Department together with the Cost Accounting Department reviews the actual Inventory tie-up every month and corrective action is taken by the Purchase Department to achieve the desired levels of inventory.

The purchase department maintains Cardex Control and order are placed to arrive at a particular approved position
every month. As such, the purchases are made against requisitions.

In the case of engineering and other consumable stores need in the plant all items, which are required to be held in the stores are by a request for inclusion in the stock list. This is recorded.

The document for inclusion in stock list is known as "addition to stock list". These documents are pre-numbered and the using departments issues them in three copies and are approved by the respective departmental heads. This is further counter-signed by the Plant Manager/Chief Engineer concerned, purchase Manager and the President. After final approval one copy is retained by the originating department, second copy is to the Purchase Department and the third copy which is known as "travelling requisition" is filled by the MRO stores. There are provisions in the card to indicate maximum and minimum stock levels, the recorder levels etc. Except when it is a first purchase, whenever stock level reaches the reorder level, stores pull out this "travelling requisition" and is routed to the using department from where it originated to determine whether further purchase of this item is necessary and also to review maximum and minimum level of stock indicated therein. This procedure of routing "travelling requisition"
is not followed for items failing under consumable stores which are repeatedly consumed in the factory. MRO stores need not to fill the third copy as travelling requisition for this. If the originating department feels it necessary that the stock must be replanished, this card is routed to the purchase department for further action.

The Purchase Department after placement of the order sends back the "travelling requisition" together with the purchase order copy meant for the stores. If, for any reasons, any particular item is not required to be reordered, the using department mentions in the "travelling requisition" the reasons for not ordering again and also state whether the quantity in stock at the time of routing the "travelling requisition" can be sold/disposed of. The using department recommends deletion of the items from the stock list, if deemed necessary. This whole system is adopted for the requisition of raw material as accounty system. If does not include in issue of raw material to the different department. Although issuing is also recorded along with these cards. Which helps in determining the level of raw material in store.
MANAGEMENT OF RECEIVABLES:

Average collection period in this company is two days. At depots and at Plant goods are delivered to the suppliers against Bank drafts or cheques drawn on local banks which takes one to two days in collection. If goods are sent to the supplier through the Bank, Company gets immediate payment from the Banks as they have DD limit facilities with the Banks upto 100 lacs. If dealer retires the documents after grace periods of seven days he is responsible for the payment of overdue interest for the delayed period.

This is a very good system and I did not any draw-back in it. System is satisfactory and suggested to be continued.
MANAGEMENT OF PAYABLE:

Except of very few suppliers which takes the money in advance before making any despatches to the paint, It is find that all other suppliers are giving credit facilities to the company ranging from 7 days to 90 days. Most of them except Rubber suppliers which are charging interest for full credit period, are giving interest free credits. Some of the suppliers have monopoly over the market. They sell their goods on their own terms. But there is no other way for the company to cope with the situation. Other suppliers are also giving their best cooperation in the smooth running of the factory by their continuous supplies. We do not see any major draw-back in the system. Payments are being made by the head office and they have a good control over the management of Receivables.