

WORKING CAPITAL MANAGEMENT AT HOTEL REXMAR LIMITED, KUMASI.

BY

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DECLARATION

I hereby declare that this submission is my own work towards the MBA and that, to the best of my knowledge, it contains no material previously published by another person nor material which has been accepted for the award of any other degree of the University, except where due acknowledgment has been made in the text.

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DEDICATION

This piece of work is dedicated to my dear parents, Mr. and Mrs. M. K. Asante and my lovely wife and child, Doreen Boamah Okyere and Daniel Opare Atuah Okyere.

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ABSTRACT

Ghana is becoming an increasingly popular destination for tourists. As one of the fastest growing sectors in the economy, tourism holds a lot of attractions for investors.

The survival and growth of hotels is an added advantage to further boost the development of the tourism sector, hence, the effective management of working capital by hoteliers will ensure that the hospitality industry have adequate resources (cash) to finance their operations.

This study analyses the working capital management efficiency of firms from the private hospitality industries, with Hotel Rexmar Ltd., as a test case. The relationship between working capital management efficiency and profitability is examined using Correlation analyses. Empirical findings of the study indicate that days of sales outstanding (DSO) and days of inventory outstanding (DIO), which are directly related variables with working capital management, have significantly negative effects on firm profitability in private hospitality industries. The following recommendations were suggested:

Addressing the issue of working capital on a corporate-wide basis has certain advantages. Cash generated at one location can well be utilized at another. For this to happen, information access, efficient corporate channels, good linkages between departments, internal systems to move cash and good cash management practices should be in place.

An innovative approach, combining operational and financial skills and an all encompassing view of the company's operations will help in identifying and implementing strategies that generate short term cash.

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Appendix

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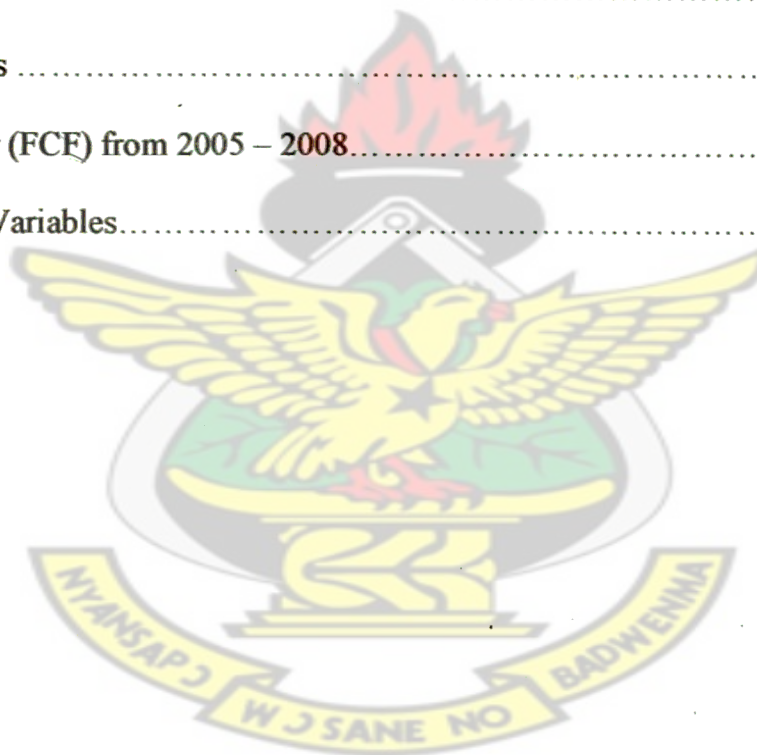


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CHAPTER ONE

1.0 INTRODUCTION TO THE STUDY AND RESEARCH CONTEXT

1.1 THE BACKGROUND TO THE STUDY

According to Ghana Investment Promotion Centre release (2008), Ghana is becoming an increasingly popular destination for tourists. As one of the fastest growing sectors in the economy, tourism holds a lot of attractions for investors. Opportunities include provision of hotel accommodation in 3 – 5 star range from Accra to other regional capitals.

According to this release, Ghana's tourism sector is expected to grow at an average of 4.1% per annum over the next two decades, driven largely by the country's unique historical, culture and natural attractions. This significant growth in the tourism sector in Ghana has attracted the development of a lot of hotel business lately.

The survival and growth of hotels will much depends on how well working capital is managed by hoteliers. This will ensure that the hospitality industry will have adequate resources (cash) to finance their operations.

Firms traditionally focused on long term capital budgeting and capital structure, the recent trend is that many companies across different industries focus on WCM efficiency. The study is therefore intended to find out how working capital is managed by management members in this particular sector and therefore its effect on the firm's profitability.

Working capital management (WCM) is the management of short-term financing requirements of a firm. This includes maintaining optimum balance of working capital components – receivables, inventory and payables – and using the cash efficiently for day-to-day operations. Optimization of working capital balance means minimizing the working capital requirements and realizing maximum possible revenues. Efficient WCM increases firms' free cash flow, which in turn increases the firms' growth opportunities and return to shareholders.

Based on this, the study further seeks to find out how management of Hotel Rexmar Ltd. applies its managerial role in the area of working capital management to improve the firm's value.

The importance of efficient working capital management (WCM) is indisputable. Business viability relies on its ability to effectively manage receivables, inventory, and payables. By minimizing the amount of funds tied up in current assets, firms are able to reduce financing costs and/or increase the funds available for expansion. Much managerial effort is put into bringing non-optimal levels of current assets and liabilities back towards their optimal levels.

The proper management of working capital helps to ensure that firms have adequate funds to finance their day-to-day activities. This will ensure that these firms can survive in the face of swift competition, generating a lot of income through profit, creating employment etc, which in effect lead to the development of the country (Ghana).

This study therefore, aims to analyze the effect of working capital management on firm's profitability, an indicator of short-term financial performance.

1.2 THE OBJECTIVES OF THE RESEARCH ARE:

- To analyze the effects of firm level characteristics on firm profitability.
- To investigate the relationship between working capital management and firm value.
- To examine whether a single key WCM component contribute to working capital management efficiency.
- To suggest ways as to how working capital management can be improved at Hotel Rexmar Ltd.

1.3 RESEARCH QUESTIONS

The primary purpose of this research is to analyze the effect of working capital management on firm profitability for the hospitality industry in the Kumasi metropolis. By identifying the proper management of working capital; the contribution this research hopes to achieve is in helping organizations to improve the successful management of their working capital. Specifically, this research study will answer the following four questions:

- 1 What are the effects of firm level characteristics on firm profitability?
2. What is the relationship between WCM and the firm's value?
3. Does a single key component contribute to working capital management efficiency?
4. What is the best working capital management practice that results in business performance success?

1.4 STATEMENT OF THE PROBLEM

Most researchers have attempted to understand the factors that determine the working capital of an organization. Horrigan (1965), Luo (1984), Liu (1985), Zhou (1995), and Su (2001) found that growth of the firm, size, and leverage etc. affect the working capital of a company. Broadly, industry characteristics, firm-specific characteristics, and the financial environment are recognized as determining factors of working capital. However, still, there are firms that are struggling to manage working capital since they don't have a sufficient understanding of the determining factors of working capital. In addition to the growth, leverage, and the size of a company, type, and size of expenditures, such as finance and operating and capital expenditures, have different impacts on working capital.

Scholars such as; Shin and Soenen (1998); Deloof (2003); Ross et al (2004); Lazaridis and Tryfondis (2006) have written extensively on working capital management in the manufacturing, IT companies and other services industries. However, not much has been done on working capital management in the hospitality industry, particularly in Ghana.

It is therefore necessary for the conduct of this study to set the pace for further research in the future.

This study is to analyse how working capital is managed at Hotel Rexmar Limited and secondly, its effects on the firm's profitability.

1.5 SIGNIFICANCE OF THE STUDY

The study will serve as guide to management of Hotel Rexmar Limited to minimize the present difficulty of poor management of working capital, thereby prevent financial failures.

The hospitality industry is growing very rapidly as a result of globalization, the attractiveness of the tourism sector among other things. This study will serve as a tool for management of Hotel Rexmar Limited in their decision –making process.

Finally, the issues this study will raise will be helpful to managers' in similar hospitality industry.

1.6 SCOPE OF THE STUDY

The study is restricted to Hotel Rexmar Limited. The focus was to study the effect of working capital management in all private hotels' profitability in the Kumasi Metropolis.

Due to time constraints the focus was narrowed down to capture only Hotel Rexmar Limited, in Kumasi. Rexmar was chosen because; it is one of the oldest Hotels in the Metropolis and represents the core of hotels in Kumasi. The researcher also realized that proper books are kept that helped in carrying out the study.

Of the entire population of about 50 employees, 15 of them were sampled for the study. First, the researcher targeted the top six (6) employees at the managerial level, because they were in the position to help with this particular study under review. But this expanded to cover nine (9) more employees after the pilot test had been carried out.

The main data used was the Audited Financial statements for the periods 2004 – 2008 (ref to appendix 1- 3). The researcher could lay hands only on this five – year financial report from the firm.

Again, the researcher wishes to find the effects of accounts receivables, inventory period, cash conversion efficiency, firm size, firm growth, current assets/total assets and leverage on the firm's profitability.

The key components of WCM for this study will cover: days of inventory outstanding, days of accounts receivables and days of accounts payables.

1.7 LIMITATION TO THE STUDY

The management of Hotel Rexmar Limited considers certain information as sensitive and therefore inaccessible to the public. Thus most of the respondents were only willing to give general information, rather than specific.

Also, the issues of confidentiality surrounding some items on the management accounts, such as cash, management members were economical with the information they provided. This made it impossible to get some vital data due to strategic role they play. It must however be noted that, in spite of these limitations, the appropriate approaches were used to minimize their effects.

Finally, the initial attempt was to carry out the study in several Hotels in the Kumasi Metropolis, but due to time constraint, attention could only be limited to Hotel Rexmar Limited.

In the future, it is the aim of the researcher to extend this study to cover more firms in this industry.

Notwithstanding these constraints, care has been taken to provide every essential detail.

1.8 ORGANISATION OF THE STUDY

This study is organised into five chapters. The first chapter is basically about the introduction and research questions. It gives the objectives of the study, states the research problem in addition to the significance, scope and the limitation to the study.

Chapter two reviews the related literature by looking at key terms such as: working capital management (WCM), working capital and firm's value, cash conversion cycle, accounts receivables management, cash management etc.

Chapter three also gives a description of the methodology of the study by looking at sample size, sampling techniques, research instrument used in the collection of data as well as the tools used to analyse the data gathered. It further gives a vivid profile of Hotel Rexmar Limited.

The fourth chapter presents the analysis and the discussion of the results based on the set objectives of the study.

Chapter five gives the summary of the findings as well as some recommendations that can help the management of Hotel Rexmar Limited in the effective and efficient decision – making process.

CHAPTER TWO

2.0 REVIEW OF RELEVANT PRIOR LITERATURE

2.1 INTRODUCTION

The importance of efficient working capital management (WCM) is indisputable. Business viability relies on its ability to effectively manage receivables, inventory, and payables. By minimizing the amount of funds tied up in current assets, firms are able to reduce financing costs and/or increase the funds available for expansion. Much managerial effort is put into bringing non-optimal levels of current assets and liabilities back towards their optimal levels.

A recent example of business attempting to maximize working capital management is the recurrent attention being given to the application of Six Sigma methodology Waxer's (2002). There appear to be many success stories, including, Towne's (2002) report of a fifteen percent increase days sales are outstanding, resulting in an increased cash flow of approximately \$2 million at Thibodaux Regional Medical Center. Furthermore bad debts declined from \$3.4 million to \$600,000. However, Waxer's (2002) study of multiple firms employing Six Sigma finds that is really a "get rich slow" technique with a rate of return hovering in the 1.2 – 4.5 % range.

Even in the world of Six Sigma, one still has to identify an "optimal" level of working capital management. Yet, what is the "optimal" working capital? Industry factors may impact firm credit policy, inventory management, and bill-paying activities. Some firms may be better suited to minimize their receivables and inventory, while others maximize their payables. Another aspect of "optimal" is the extent to which poor financial results can be tied to sub-optimal performance. Are firms with more "efficient" inventory management thereby reducing inventory to such an extent that sales are not lost? Fortunately, these issues are testable with data published by *CFO* magazine,

which claims to be the source of “tools and information for the financial executive,” and are the subject of this research REL Consultancy (2005).

2.2 WORKING CAPITAL MANAGEMENT

According to Home (1977), working capital management is the administration of current assets in the name of cash, marketable securities, receivables, and inventories. Osisioma (1997) described working capital management as the regulation, adjustment, and control of the balance of current assets and current liabilities of a firm such that maturing obligations are met, and the fixed assets are properly serviced. In order to manage working capital efficiently, there must exist two elements as necessary components and desirable quantities. Osisioma (1997) demonstrated that good working capital management must ensure an acceptable relationship between the different components of a firm's working capital so as to make an efficient mix, which will guarantee capital adequacy. Thus, working capital management should make sure that the desirable quantities of each component of the working capital are available for management. However the question is "What determines the necessary components of a firm's working capital and how much of such necessary components can be regarded as adequate or desirable?"

2.2.1 Components of Working Capital

The necessary components of an organization's working capital, basically, depend on the type of business and industry. Cash, debtors, receivables, inventories, marketable securities, and redeemable futures can be recognized as the common components of organization's working capital. However, the question is to recognize the factors that determine the adequacy of working capital based on growth, size, operating cash flow, etc. The inability to understand the determining

factors and measurement of adequate amounts of working capital will lead an organization to bankruptcy.

Another component of working capital is accounts payable, but it is different in the sense that it does not consume resources; instead it is often used as a short term source of finance. Thus it helps firms to reduce its cash operating cycle, but it has an implicit cost where discount is offered for early settlement of invoices.

1.2.2 Working Capital Decisions

Corporate finance basically deals with three decisions: capital structure decisions, capital budgeting decisions, and working capital management decisions. Among these, working capital management is a very important component of corporate finance since it affects the profitability and liquidity of a company. It deals with current assets and current liabilities which was an important concern of the financial manager due to many reasons? For one thing, a typical manufacturing firm's current assets account for over half of its total assets. For a distribution company, they account for even more. The maintenance of excessive levels of current assets can easily result in a substandard return on a firm's investment. However, firms with inadequate levels of current assets may incur shortages and have difficulties in smoothly maintaining day-to-day operations (Home and Wachowicz, 2000). Efficient working capital management involves planning and controlling current assets and current liabilities in a manner that eliminates the risk of inability to meet due short term obligations on one hand and avoids excessive investment in these assets on the other hand (Eljelly, 2004).

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Many exiting research papers have found that managers spend a considerable time on day-today working of capital decisions since current assets are short-lived investments that are continually being converted into other asset types (Rao, 1989). In the case of current liabilities, the firm is responsible for paying obligations mentioned under current liabilities on a timely basis. Liquidity for the on-going firm is reliant, rather, on the operating cash flows generated by the firm's assets (Soenen, 1993). As a result, working capital management of a company is a very sensitive area in the field of financial management (Joshi, 1994). Joshi iterates that WCM involves the decisions about the amount and composition of current assets and the financing of these assets. The decision-making process on the level of different working capital components has become frequent, repetitive, and time-consuming.

2.2.3 Determinants of Working Capital

Corporations are looking for new ways to stimulate growth, improve financial performance, and reduce risk in today's challenging economic climate. Funds tied up in working capital can be seen as hidden reserves that can be used to fund growth strategies, such as capital expansion. Cash flows locked in stock and receivables can be freed up by understanding the determinants of working capital. Many organizations that have earned profits over the years have shown the efficient management of working capital (WCM). The successful management of working capital is essential for short-run corporate solvency or the survival of any organization. Especially, efficient WCM will lead a firm to react quickly and appropriately to unanticipated changes in market variables, such as interest rates and raw material prices, and gain competitive advantages over its rivals. Too often, however, this is an area that many organizations have ignored. The way of managing working capital efficiently varies from firm to firm since it depends on industry, the

nature of the business, business policy, strategy, etc. Thus, it is very important for an organization to understand the way to manage working capital efficiently.

Most researchers have attempted to understand the factors that determine the working capital of an organization. Horrigan (1965), Luo (1984), Liu (1985), Zhou (1995), and Su (2001) found that growth of the firm, size, and leverage etc. affect the working capital of a company. Broadly, industry characteristics, firm-specific characteristics, and the financial environment are recognized as determining factors of working capital. However, still, there are firms that are struggling to manage working capital since they don't have a sufficient understanding of the determining factors of working capital. In addition to the growth, leverage, and the size of a company, type, and size of expenditures, such as finance and operating and capital expenditures, have different impacts on working capital.

2.3 NATURE OF WORKING CAPITAL

The working capital meets the short-term financial requirements of a business enterprise. It is a trading capital, not retained in the business in a particular form for longer than a year. The money invested in it changes form and substance during the normal course of business operations. The need for maintaining an adequate working capital can hardly be questioned. Just as circulation of blood is very necessary in the human body to maintain life, the flow of funds is very necessary to maintain business. If it becomes weak, the business can hardly prosper and survive. Working capital starvation is generally credited as a major cause if not the major cause of small business failure in many developed and developing countries (Rafuse, 1996).

The success of a firm depends ultimately, on its ability to generate cash receipts in excess of disbursements.

The cash flow problems of many small businesses are exacerbated by poor financial management and in particular the lack of planning cash requirements (Jarvis et al, 1996).

2.4 THE MANAGEMENT OF WORKING CAPITAL

While the performance levels of small businesses have traditionally been attributed to general managerial factors such as manufacturing, marketing and operations, working capital management may have a consequent impact on small business survival and growth (Kargar and Blumenthal, 1994). The management of working capital is important to the financial health of businesses of all sizes. The amounts invested in working capital are often high in proportion to the total assets employed and so it is vital that these amounts are used in an efficient and effective way. However, there is evidence that small businesses are not very good at managing their working capital. Given that many small businesses suffer from undercapitalization, the importance of exerting tight control over working capital investment is difficult to overstate (Kargar, 1994).

A firm can be very profitable, but if this is not translated into cash from operations within the same operating cycle, the firm would need to borrow to support its continued working capital needs. Thus, the twin objectives of profitability and liquidity must be synchronized and one should not impinge on the other for long. Investments in current assets are inevitable to ensure delivery of goods or services to the ultimate customers and a proper management of same should give the desired impact on either profitability or liquidity. If resources are blocked at the different stage of the supply chain, this will prolong the cash operating cycle. Although this might increase profitability (due to increase sales), it may also adversely affect the profitability if the costs tied up in working capital exceed the benefits of holding more inventory and/or granting more trade credit to customers (Kargar and Blumenthal, 1994).

Although working capital is the concern of all firms, it is the small firms that should address this issue more seriously. Given their vulnerability to a fluctuation in the level of working capital, they cannot afford to starve of cash. The study undertaken by Peel *et al.*, (2000) revealed that small firms tend to have a relatively high proportion of current assets, less liquidity, exhibit volatile cash flows, and a high reliance on short-term debt.

2.4.1 Inventory Management

Both accounts receivable and inventory management are key success variables to efficient working capital management strategies. Nike CEO Philip Knight singled out inventory as the most important issue on which Nike's long-term fate relies. He noted that in order "to protect margins and brand value, the company needs to manage its inventory better" (Fredeen, 2000). A 2004 Business Week cover story (Holmes and Bernstein, 2004) indicated that Nike had made significant changes by focusing on, as one Nike insider, stated, "the basic pieces of the business: operating principles, financial management, supply-chain renovation and inventory management."

2.4.2 Accounts Receivables Management

The nature of the receivables challenge varies from region to region but in 2004, many corporations were still grappling with collection challenges that create serious working capital issues and negatively impact their bottom line. For instance, corporations that are not paid in a timely way frequently need funding and credit to build and deliver goods, and sales representatives often waste a significant amount of time disputing individual line items on invoices with customers rather than selling to them. This is particularly evident in Latin America. Electronic Invoice Presentment and Payment applications, which are gaining momentum around the world and are

becoming more innovative, has become an effective working capital tool, helping to mitigate regional collection inefficiencies (Rule, 2004).

The two primary concerns firms have regarding receivables are the lost cash flows arising from bad debts and from administrative costs. Sanchez (1992) surveys over 8,000 firms and finds that on average 25 percent of receivables are delinquent at any given time. He also finds that less than one percent of delinquent receivables are ever written off as a loss. As a result, he views collections not so much as enforcement of payment but more as "the process of completing the sale." He argues that internal processes are critical to accounts receivable management.

The Vengroff, Williams and Associates (VWA) survey (2009) revealed that a large number of the companies are significantly concerned about both cash flow and tight liquidity and are keeping a strident watch on credit terms and corporate credit risk. The global economic environment and restricted access to liquidity have highlighted the importance of an efficient cash management structure. As working capital is the lifeblood of firms, 90% of the survey respondents indicated that they are constantly examining the ways in which they can get cash flow under control. While traditional corporate performance levels have focused on factors such as the efficiency of manufacturing, operations, and the effectiveness of sales and marketing, the primary issue in working capital management, is to dictate business survival and growth.

Additionally, the survey revealed that historical-based measurements, such as past due percentages, days in sales outstanding (DSO) and aging quality, used by 89% of the responding companies, are the primary measures of success for their firms. The majority of those polled stated that they are looking for proactive ways to head off receivables disputes before they become an issue.

Furthermore, 90% of the polled corporations agree that effective dispute and deduction management can improve customer service and unlocks time for justifiable activities like sales, order entry and cash collection. Overall, with effective working capital processes in place, efficiency increases as a result of reduced operating costs. In fact, 72% of respondents say that their company reviews the balance of overdue receivables on a weekly basis.

Regarding minimizing administrative costs, Smith and Belt (1989) report that most of the respondents of the Fortune 1000 companies that were surveyed used more than one method of determining to whom to grant credit and monitor customers' payment behaviours. Beranek and Sherr (1991) find that 58 percent of the respondents to their survey establish credit limits for over 90 percent of their customers. Also, the vast majority of firms that responded to a survey by Byl (1994) use more than one method to report the status of their receivables to management. All methods employed by firms to control accounts receivable increase administrative costs and, if not successful, hurt the bottom line.

Ricci (1999) surveys 200 randomly-selected credit managers on the topics of pre-sale issues, post-sale issues, and reporting issues. Although Ricci finds that several methods were being used to identify creditworthy customers, using multiple methods did not have an impact on the level of past due accounts. Furthermore, no relationship existed between the amount of money spent on information and the percentage of sales turning into bad debts. Despite this, a majority of the firms in the survey were willing to pay higher investigation costs as the size of potential sales increased. According to Ricci's survey, one factor that did tend to reduce the number of past-due accounts was the effective setting of credit limits.

As part of a study of the Fortune 500's financial management practices, Gilbert and Reichert (1995) find that time value of money cash flow analysis is used to select projects in 91 percent of the firms. Accounts receivable management models are used in 59 percent of these firms, while inventory management models were used in 60 percent of the companies. Recently, Farragher, Kleiman and Sahu (1999) find that 55 percent of firms in the S&P Industrial index complete some form of a cash flow assessment, but did not present insights regarding accounts receivable and inventory management, or variations of any current account asset or liability accounts across industries.

2.4.3 Accounts Payables Management

Most firms have a large amount of cash invested in working capital, as well as substantial amounts of short-term payables as a source of financing. For instance, according to the National Bank of Belgium, in 1997 accounts receivable and inventories were respectively 17% and 10% of total assets of all Belgian non-financial firms. Accounts payable were 13% of total assets of these firms. It can be expected that the way in which working capital is managed will have a significant impact on the profitability of firms. Accordingly, for many firms working capital management (WCM) is a very important component of their financial management.

Firms may have an optimal level of working capital that maximizes their value. On the one hand, large inventory and a generous trade credit policy may lead to higher sales. Larger inventory reduces the risk of a stock-out. Trade credit may stimulate sales because it allows customers to assess product quality before paying (Long, Malitz and Ravid, 1993; Deloof and Jegers, 1996). Because suppliers may have significant cost advantages over financial institutions in providing credit to their customers, it can also be an inexpensive source of credit for customers (Petersen and

Rajan, 1997). The flip side of granting trade credit and keeping inventories is that money is locked up in working capital.

Another component of working capital is accounts payable. Delaying payments to suppliers allows a firm to assess the quality of the products bought, and can be an inexpensive and flexible source of financing for the firm. On the other hand, late payment of invoices can be very costly if the firm is offered a discount for early payment. In a 1996 survey of trade credit policies in Europe, Svensson (1997) found that 75% of Belgian firms offered a discount for prompt payment, and the average discount offered was 3%. For all European firms in the survey, the average payment period was 61 days and 54% of the firms offered a discount that was on average 4%.

A popular measure of WCM is the cash conversion cycle, i.e. the time lag between the expenditure for the purchases of raw materials and the collection of sales of finished goods. The longer this time lag, the larger the investment in working capital. A longer cash conversion cycle might increase profitability because it leads to higher sales. However, corporate profitability might also decrease with the cash conversion cycle, if the costs of higher investment in working capital rise faster than the benefits of holding more inventories and/or granting more trade credit to customers. Shin and Soenen (1998) investigate the relation between a measure of the cash conversion cycle and corporate profitability. For a large sample of listed American firms for the 1975-1994 periods, they find a strong negative relation. This result indicates that managers can create value for their shareholders by reducing the cash conversion cycle to a reasonable minimum.

2.4.4 Cash Management

Sorab and Sharukh (2006), argue that too much cash is not good nor is having too little a healthy practice. They iterate that, good companies usually have a practice to plant surplus cash in risk free securities or intercompany deposit. On the other hand, companies with a deficit tend to borrow at a high rate of interest indicating a lack of planning. A sudden surge in business may spur the need of working capital and this may also require additional interest to be paid and again planning is important.

A firm is required to maintain a balance between liquidity and profitability while conducting its day to day operations. Liquidity is a precondition to ensure that firms are able to meet its short-term obligations and its continued flow can be guaranteed from a profitable venture. The importance of cash as an indicator of continuing financial health should not be surprising in view of its crucial role within the business. This requires that business must be run both efficiently and profitably. In the process, an asset-liability mismatch may occur which may increase firm's profitability in the short run but at a risk of its insolvency. On the other hand, too much focus on liquidity will be at the expense of profitability and it is common to find finance textbooks (Gitman, 1984 and Bhattacharya, 2001) begin their working capital sections with a discussion of the risk and return tradeoffs inherent in alternative working capital policies. Thus, the manager of a business entity is in a dilemma of achieving desired tradeoff between liquidity and profitability in order to maximize the value of a firm.

2.5 EMPIRICAL ANALYSIS

2.5.1 Efficient Working Capital Management

The recent work of Howorth and Westhead (2003), suggest that small companies tend to focus on some areas of working capital management where they can expect to improve marginal returns. For small and growing businesses, an efficient working capital management is a vital component of success and survival; i.e. both profitability and liquidity (Peel and Wilson, 1996). They further assert that smaller firms should adopt formal working capital management routines in order to reduce the probability of business closure, as well as to enhance business performance. The study of Grablowsky (1976) and others have showed a significant relationship between various success measures and the employment of formal working capital policies and procedures.

Managing cash flow and cash conversion cycle is a critical component of overall financial management for all firms, especially those who are capital constrained and more reliant on short-term sources of finance (Walker and Petty, 1978; Deakins et al, 2001). Given these peculiarities, Peel and Wilson (1996) have stressed the efficient management of working capital, and more recently good credit management practice as being pivotal to the health and performance of the small firm sector. Along the same line, Berry et al (2002) finds that SMEs have not developed their financial management practices to any great extent and they conclude that owner-managers should be made aware of the importance and benefits that can accrue from improved financial management practices. The study conducted by Mee (1998) revealed that 60% enterprises suffer from cash flow problems.

Narasimhan and Murty (2001) stress on the need for many industries to improve their return on capital employed (ROCE) by focusing on some critical areas such as cost containment, reducing

investment in working capital and improving working capital efficiency. The pioneer work of Shin and Soenen (1998) and the more recent study of Deloof (2003) have found a strong significant relationship between the measures of WCM and corporate profitability. Their findings suggest that managers can increase profitability by reducing the number of days of accounts receivable and inventories. This is particularly important for small growing firms who need to finance increasing amounts of debtors.

2.5.2 Working Capital Management for Value

A review of prior literature reveals little evidence on the consequences of working capital management for firm value or what factors influence a firm's management of its working capital. This state of affairs is surprising for two reasons. First, practically every corporate finance textbook devotes attention to corporate working capital management and the issues that it raises. Second, corporations appear to pay a great deal of attention to how well they are doing in managing their working capital. For example, REL Consultancy Group has for years conducted an annual survey of corporate working capital management performance for CFO Magazine, (CFO Magazine, 2005).

As the 2005 U.S. survey report points out, there is a high positive correlation between the efficiency of a corporation's working capital policies and its return on invested capital. Both issues examine: what are the consequences of working capital management for firm value, and what factors influence a firm's working capital management performance. How important these issues can be is illustrated by a couple of examples. First, Shin and Soenen (1998) point out that Wal-Mart and Kmart had similar capital structures in 1994, but because Kmart had a cash conversion

cycle of roughly 61 days while Wal-Mart had a cash conversion cycle of 40 days, that Kmart likely faced an additional \$198.3 million per year in financing expenses. Clearly Kmart's poor management of its working capital contributed to its going bankrupt. Second, IT world (2002) recently posted the results of a study arguing that poor working capital management practices cost IT companies billions of dollars annually. Mirroring this conclusion, REL (2005) *Working Capital Survey* concludes that U.S. corporations had roughly \$460 billion unnecessarily tied up in working capital.

2.5.3 Investment in Working Capital

Using data on a panel of U.S. corporations from 1990 through 2004, evidence revealed a significantly negative relationship between firm value and investment in working capital that is consistent with over-investment in working capital. Such a conclusion is not only consistent with the above mentioned IT world.com survey, but also the conclusions in different annual surveys of U.S. corporate working capital management performance by REL (2005) Consultancy for *CFO Magazine*. Turning to what influences a firm's management of working capital, it was found that a firm's working capital policy is influenced by its industry's working capital policies, its size, its expected sales growth, the proportion of outside directors on its board, the current compensation of its CEO, and its CEO's share ownership. Consequently, managerial incentives and the monitoring of management are significant influences on a firm's working capital management performance.

Shin and Soenen (1998) point out that a corporation's working capital is the result of the time lag between the expenditure for the purchase of raw materials and the collection from the sale of finished goods. As such, it involves many different aspects of corporate operational management: management of receivables, management of inventories, management and use of trade credit, etc.

Consequently, there are streams of research on individual aspects of working capital management (Petersen and Rajan (1997)), but such literature ignores the joint effect of these individual policies, which is often a focal point of corporate concern. For this reason, the discussion is limited to the prior literature that focuses on overall working capital management: its causes and consequences.

2.5.4 Effect of WCM on Firm's Value

With respect to the effect of working capital management on firm value, only one published study was found to examine the relationship between a firm's working capital management and its accounting profitability. Shin and Soenen (1998) examine the relation between different accounting profitability measures and net trade cycles, a summary efficiency measure of a firm's working capital management. Shin and Soenen's evidence implies that firms that manage their working capital more efficiently (i.e., shorter net trade cycle) experience higher operating cash flow and are potentially more valuable. However, this last implication does not necessarily follow because firms that have net trade cycles are also investing in short-term assets which may pay off in subsequent periods. So the valuation issue is whether such investment earns a return above the cost of capital.

As for the determinants of working capital practices, even less prior research on which to draw. Nunn (1981) uses the PIMS database to examine why some product lines have low working capital requirements, while other product lines have high working capital requirements. In addition, Nunn is interested in "permanent" rather than temporary working capital investment as he uses data averaged over four years. Using factor analysis, he identifies factors associated with the production, sales, competitive position, and industry. Reinforcing the role of industry practices on

firm practices, Hawawini, Viallet, and Vora (1986) examine the influence of a firm's industry on its working capital management. Using data on 1,181 U.S. firms over the period 1960 to 1979, they conclude that there is a substantial industry effect on firm working capital management practices that is stable over time. From these studies, conclusion was that sales growth and industry practices are important factors influencing a firm's investment in working capital.

What the above review illustrates is that there is scant evidence on the effect of investment in working capital on firm value, and little evidence on what factors influence a firm's management of working capital, particularly as they relate to corporate governance. Consequently, we turn to our examination of these issues.

The importance of cash flow is not new to the finance literature. Over twenty years ago, Largay and Stickney (1980) reported that the then-recent bankruptcy of W.T. Grant, a nationwide chain of department stores, should have been anticipated because the corporation had been running a deficit cash flow from operations for 8 of the last 10 years of its corporate life.

Theoretical determination of optimal trade credit limits are the subject of many articles over the years (e.g., Schwartz, 1974 and Scherr, 1996), with scant attention paid to actual accounts receivable management. Across a limited sample, Weinraub and Visscher (1998) observe a tendency of firms with low levels of current ratios to also have low levels of current liabilities. Combining accounts receivable and payable into one issue is Hill, Satoris, and Ferguson's (1984) finding that payees define date of payment as the date payment is received, while payers view payment as the postmark date.

Additional WCM insight across firms, industries, and time is needed! Maness and Zietlow (2002,) present two models of value creation through effective short-term financial management activities. However, these models are generic models and do not consider unique firm or industry influences.

Maness and Zietlow discuss industry influences in a short paragraph that includes the observation that “An industry a company is located in may have more influence on that company’s fortunes than overall GNP” (2002,).” In fact, a careful review of this 627-page textbook finds only sporadic information on actual firm levels of WCM dimensions, virtually nothing on industry factors except for some boxed items with titles such as “Should a Retailer Offer an In-House Credit Card”, and nothing on WCM stability over time.

2.6 OPERATING ASSETS AND LIABILITIES

The commitment of funds to fixed assets is readily understandable as an investment, due to its strategic nature and long economic life of such assets. Unlike the case of fixed assets, it is easy to overlook the importance of managing the level of investment in working capital (Lewellen, Halloran and Lanser, 2006). They iterated that since working capital consists of current assets, the short – life of these assets seems to preclude viewing this use of funds as an investment.

Furthermore, current assets seem to arise automatically from operations. As sales rise and fall, the level of inventories needed to support sales and the level of receivables arising from credit sales would seem also to fluctuate independent of management control (Lewellen 2006). This view point is overly simplistic. It is true that the investment in current assets will fluctuate over time in response to changes in sales. Financial managers, however, can alter the level of current assets associated with a given volume of sales at any point in time. Policy decisions regarding inventories, accounts receivables, cash balances and marketable securities can control the amount invested.

Lewellen et al (2006) believe that, if a firm’s managers are to select the level of current assets that is optimal, they must have a goal to guide their decision – making: maximize the value of the firms

to its owners. This they affirm that working capital decisions affect value by altering either the size of free cash flow or RRR at which they are discounted.

Although working capital consists of current assets, it is not true that working policy deals with only short –term assets. In fact, many of the dollar balance in current assets accounts that are classified as short – term within an accounting frame – work are as long –lived as fixed assets from the financial manager view point. The same statement can be made about a firm's current liabilities. From the perspective of the financial managers, many current liabilities represent long – term debt financing (Lewellen et al., 2006).

2.7 WORKING CAPITAL AND LONG TERM VALUE CREATION

A focus on working capital can help management drive transparency and accountability throughout the organisation. Most companies focus on reducing debtor days and bringing down inventory instead of a whole-of-business-approach to working capital.

Many organisations are struggling to understand and institutionalise the cultural and structural changes to enable long term benefits from working capital reduction.

Focusing on working capital provides managers with the opportunity to create lasting value.

Working capital is a lens through which management can examine their organization's productivity and efficiency. Implemented correctly, working capital management will make companies stronger tomorrow than they are today (Deloitte 2009).

In order to permanently improve working capital, companies need to take a cross-organisational view of the cash conversion cycle including purchase to pay, forecast to fulfillment and order to cash. They need to break down and scrutinise the individual components of the entire supply chain and then piece it back together in a way that creates a lasting step change in cash efficiency. This

enables companies to refocus away from purely growth-oriented processes which were developed during the economic boom towards more cash efficient ways of doing things.

2.8 CASH CONVERSION CYCLE AND FIRM'S PROFITABILITY

Cash conversion cycle as a part of operating cycle (Fig.1) is an ongoing liquidity measure developed by Gitman (1974). Closely related with operating cycle, cash conversion cycle is, in brief, the part of operating cycle financed by the firm itself (McLaney, 1997) and is simply calculated by adding inventory period to accounts receivables period and then subtracting accounts payables period from it. It focuses on the length of time between the acquisition of raw materials and other inputs and the inflow of cash from the sale of goods (Arnold, 1998). The shorter this cycle, the fewer resources the firm needs to tie up.

Traditional approach to interaction between cash conversion cycle and profitability posits that, relatively long cash conversion periods tend to decrease profitability. Trade activities of a firm can be considered as a process in circulation where cash is converted into assets and assets into cash. Cash available for trade activities of the firm has an important multiplier effect due to its turnover ratio. Higher cash turnover ratios enable managers to minimize short-term investments whose rates of return are relatively lower compared to long-term investments and consequently increase profitability.

Studies regarding working capital are mostly related with improving models to determine optimal liquidity and cash balance, rather than analyzing underlying reasons of relationships between liquidity, working capital management practices and profitability. Pioneer studies of Baumol (1952) about an inventory management model and of Miller (1966) about a cash management

model may be considered as the best-known studies in this field. Though foundations and assumptions of these models are not well-established in terms of applicability, they inform managers about problems related with working capital management practices. Later on, Johnson and Aggarwal (1998), similarly, have developed a cash management model focusing on cash flows and argued that cash collection and cash payment processes should have to be handled independently.

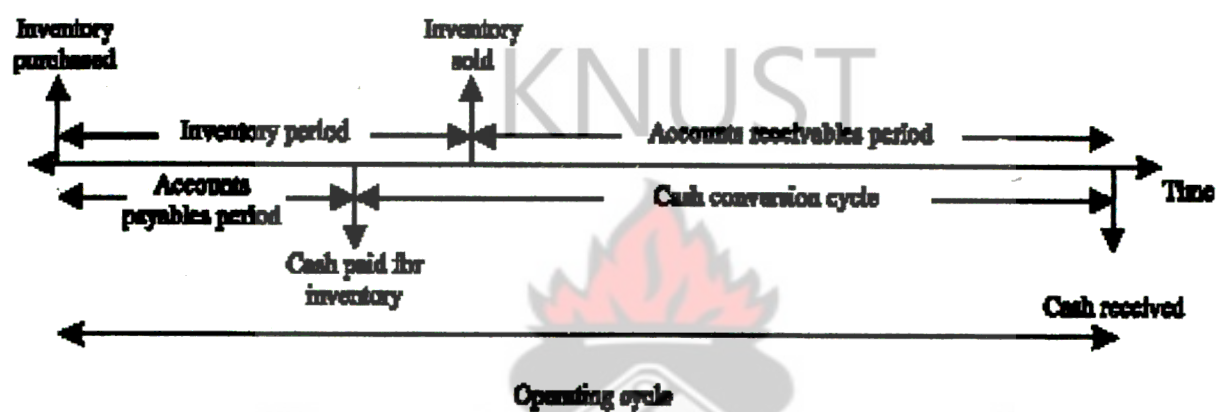


Fig. 1: Operating and cash conversion cycles. Fundamentals of corporate finance (Ross *et al.*, 2003)

As mentioned before, traditional measures of liquidity are in lack of expressing the effects of cash flows; hence, the effectiveness (and quality) of working capital management practices in terms of firm profitability should be revised by components of cash conversion cycle. Literature review consisting some of previous studies -though limited in scope and outnumbered-regarding with the relationship between profitability and working capital management practices is given below.

In a study by Kamath (1989) about working capital management practices in retailing firms, it has been concluded that there is a reverse relationship between cash conversion cycle and profitability. The results of a more detailed study by Soenen (1993) have shown that, in case of overlooking industrial differences, there does not exist any statistically constant relationship between cash

conversion cycle and profitability. However, in case of considering industrial differences, the relationship between the mentioned variables has shown dissimilarities across industries as positive in some industries and negative in others. In another study of Shin and Soenen (1998), a sample consisting of American manufacturing firms for the period of 1974-1995 has been analysed and a statistically negative relationship between cash conversion cycle and profitability has been confirmed. In a similar study to our study, Deloof (2003) has discussed possible relationships between cash conversion cycle and profitability by dividing cash conversion cycle into its components (inventory, accounts receivables and accounts payables periods). Results of the study have concluded that increases in all of these periods affect profitability negatively. Empirical findings of Lazaridis and Tryfonidis (2006) 's study have been similar to Deloof (2003)'s. According to the results of their study based on a sample of 131 Athens Stock Exchange listed companies for the period of 2001-2004, cash conversion cycle affects profitability negatively. According to the findings of another study from a different perspective, it has been concluded that the effect of cash conversion cycle on profitability is stronger than the effect of current ratio on it (Eljelly, 2004).

2.9 MEASURE OF LIQUIDITY

2.9.1 Traditional versus Cash Conversion Cycle (CCC)

In general, it is possible to discuss finance theory under three main threads as capital budgeting, capital structure and working capital management. The first two of them are mostly related with financing and managing long-term investments. However, financial decisions about working capital are mostly related with financing and managing short-term investments and undertake both current assets and current liabilities simultaneously (Mueller, 1953; Scherr, 1989; Moyer *et al.*,

1992; Pinches, 1992; Brealey and Myers, 1996; Brigham and Gapenski, 1996; Damodaran, 2002; Aksoy, 2005). So, most of the time, it is reasonable to term short-term financial management as working capital management (Ross *et al.*, 2003).

Efficiency in working capital management is so vital for especially production- firms whose assets are mostly composed of current assets (Horne and Wachowitz, 1998) as it directly affects liquidity and profitability of any firm (Raheman and Nasr, 2007). According to Kargar and Bluementhal (1994) bankruptcy may also be likely for firms that put inaccurate working capital management procedures into practice, even though their profitability is constantly positive. Hence, it must be avoided to recede from optimal working capital level by bringing the aim of profit maximization in the foreground, or just in direct contradiction, to focus only on liquidity and consequently pass over profitability. While excessive levels of working capital can easily result in a substandard return on assets; inconsiderable amount of it may incur shortages and difficulties in maintaining day-to-day operations.

2.9.2 Working Capital as Major Source of Capital

Working capital is also a major external source of capital for especially small and medium sized and high-growth firms. These firms have relatively limited access to capital markets and tend to overcome this complication by short-term borrowing. Working capital position of such firms is not only an internal firm-specific matter, but also an important indicator of risk for creditors (Moyer *et al.*, 1992). Higher amount of working capital enables a firm to meet its short-term obligations easier. This results increase in borrowing capability and decrease in default risk (and consequential decrease in cost of capital and increase in firm value). So, it is possible to state that efficiency in

working capital management affects not only short-term financial performance (profitability), but also long-term financial performance (firm value maximization).

2.9.3 Liquidity – An Important Factor in Determining WCM Policies

Liquidity, as a function of current assets and current liabilities, is an important factor in determining working capital policies and indicates firm's capability of generating cash in case of need. Current, acid-test and cash ratios as traditional measures of liquidity are incompetent and static balance sheet based measures that cannot provide detailed and accurate information about working capital management effectiveness (Finnerty, 1993; Jose *et al.*, 1996). Formulas used for calculating them consider both liquid and operating assets in common. However, considering operating assets like receivables and inventories with cash and cash-equivalent assets is illogical for basic principles of cash management. Besides, mentioned traditional ratios are also not meaningful in terms of cash flows (Richards and Laughlin, 1980).

Drawing attention to limitations of traditional liquidity ratios, Hager (1976), Richards and Laughlin (1980), Emery (1984a), Kamath (1989), Gentry *et al.* (1990), Schilling (1996) and Boer (1999) have insisted on using ongoing liquidity measures in working capital management. Ongoing liquidity refers to the inflows and outflows of cash through the firm as the product acquisition, production, sales, payment and collection process takes place over time. As the firm's ongoing liquidity is a function of its cash (conversion) cycle (Pinches, 1992), it will be more appropriate and accurate to evaluate effectiveness of working capital management by cash conversion cycle, rather than traditional liquidity measures.

CHAPTER THREE

3.0

METHODOLOGY

3.1 RESEARCH DESIGN AND STRATEGY

Saunders et al (1997) define Research strategy as general plan of how the researcher will go about answering the research question(s) posed. It is concerned with the overall approach to be used in conducting the research. Robson (1993) lists the three traditional research strategies as:

- Experiment
- Survey
- Case study

For the purpose of this study, a case study research strategy is adopted. The case study has been accepted as a viable research tool partly because people want a convenient and meaningful technique to capture a time – framed picture of the research being undertaken (Merriam,1998). Case studies also appeal to people because they have 'face – value credibility', that is , they can be seen to provide evidence or illustrations with which some readers can readily identify (Bassegy,1999).

The case study is an ideal methodology when a holistic, in-depth investigation is needed (Feagin et al, 1991), and it is of particular interest if the researcher wishes to gain a rich understanding of the context of the research and the process being enacted (Morris and Wood, 1991).

This case study approach is preferable for this research, because it enables the researcher to examine why the company's administration of working capital may have an important impact on the profitability and liquidity of the firm (Shin and Soenen, 1998).

The study is to analyse the effect of working capital management on firm's profitability" and the following methods were used in collecting and analyzing of data.

Information for this study was gathered through the study of documentations, questionnaire administration, and telephone interview, depending on the location of the respondent at the time of the study.

The rationale for choosing the telephone interview was to enable management members who are too busy to be engaged for lengthy periods respond through the telephone interview. Other staff were given the questionnaires to respond to at their own convenience and when they are more emotionally balanced.

3.2 POPULATION AND SAMPLE SIZE

The focus was to study the effect of working capital management in managerial work in all private hotels in the Kumasi Metropolis. Due to time constraints the focus was narrowed down to capture only Hotel Rexmar Limited, in Kumasi.

Of the entire population of about 50 employees, 15 of them were sampled for the study. First, the researcher targeted the employees at the managerial level, who are made up of six (6) because they were in the position to help with this particular study under review.

Second, a simple random sample technique was used to select the respondents from the employees at the top level of management for the administering of the questionnaires.

This technique was used because; it helped to get a true representative of the respondents from all the departments.

3.3 DATA COLLECTION

In accordance with the set objective of the study the following sources were used to gather the information needed:

1. Documentation – including financial statements, study reports and management reports.
2. Interviews – one of the most important sources of case study information. It took the form of open-ended and focused. The Accountant and the Managing Director were interviewed. The Interview Guide is attached as Appendix 4(b).
3. Questionnaire – questionnaires were administered on behalf of the researcher by an agent.

In this study, questionnaire (primary data) and documentary analysis (secondary data) such as financial statements and management reports were used.

3.3.1 Secondary Data

The researcher conducted a detailed research of secondary data on the following lines:

1. Analysis of the annual audited accounts (financial statements) for the five years, 2004 – 2008.
2. Analysis and interpretation of the cash flow statements for the period 2004 – 2008.
3. Application of financial ratios, which are commonly used in assessing the liquidity of firms because they are easy to understand and interpret.

4. Analysis of the liquidity trends and cash flow statements involved the extensive use of spreadsheets.

While such accounting sources were useful for analytical insights, they were not adequate to complete the analytical thrusts of the study. The following documents were therefore used to support the study.

- (i) Company's policy on working capital management practices to evaluate the liquidity measures.
- (ii) Directors' and Auditors' reports on the financial statements for the said years, paying attention to issues relating to working capital management.
- (iii) Analysis of the monthly and quarterly management reports of the company for 2004 – 2008.

The five – year financial reports of the firm were used in the study because, they were the only ones the researcher was able to lay hands on. Accordingly, five years' financial reports were quite adequate for the study.

3.3.2 Primary Data

To supplement the secondary research activities described above, information was gathered from the top management namely: Managing Director, Accountant, Marketing manager and the Operations Manager. Accordingly questionnaires were administered to fifteen employees, a sample of which is attached as Appendix 5(a).

3.3.3 Questionnaire Design

The questionnaire was designed to provide both qualitative and quantitative information on the prevailing working capital management practices in the company and to allow appropriate conclusions and recommendations to be derived. The questionnaire covered the following major areas:

- (i) The company's policy for working capital management
- (ii) The structure of the company's working Capital management
- (iii) The company's financial performance
- (iv) The company's cash management practices
- (v) The management of the components of the company's working (Strategies, Methodologies and Management)
- (vi) The sources and financing structure of the company's working capital

3.3.4 Measures

The questionnaire used in this study comprises a combination of ordinal scales, closed question responses and request for factual information.

- (i) **Ordinal scales:** These were used in the questionnaire because they have the advantage of converting a qualitative into quantitative response. Another benefit of ordinal scales is that they are ranking scales that have the ability to determine a single attribute and allow statistical calculations to be made.
- (ii) **Closed questions:** Both dichotomous and multiple choice, were used. The main benefit of a dichotomous closed question is the 'clear cut' response it offers but its downside is that it 'polarises' the required responses. The benefit of a multiple choice closed

question is that a 'menu' of answers are provided that requires one response and therefore overcomes the 'polarity' of dichotomous closed questions.

- (iii) **Open questions:** Some follow up questions were open – ended questions. These give respondents the opportunity to volunteer information and comments rather than limiting them to the researcher's opinions supplied. The major advantage of open questions is that they promote the free flow of information while its downside lies in the difficulty of analysis and statistical treatment of the responses.

All the data needed could have been gotten from the Managing director, Accountant and any other functional head through the conduct of interview but the researcher decided to go beyond them.

The reason is that such managers always decide to give only the fine story. The purpose of this approach was to get the real information beyond such fine stories given by top managers. Again, a lot of information could have been gotten from the Audited Financial Statements from 2004 – 2008, but the purpose once again was to gather information beyond the figures.

3.4 PILOT TESTING

A pilot questionnaire were first administered to three top management members namely; Managing Director, Accountant and the Marketing Manager that helped in fine tuning the questions to suite the purpose of the study. The initial questionnaires were made up of 30 items but the pilot test helped to expand it to the current form. It became necessary for further follow up questions to capture more variables for the conduct of the study.

Furthermore, the researcher wanted to find out whether the information gathered translates into the figures provided by the financial report. In all, the Questionnaires were made up of 40 items.

In all thirteen (13) questionnaires administered to respondents were returned representing 65%. Two of the respondents namely; the Managing Director and Marketing Manager were out of the country as at the time of collection.

The questionnaires were administered by the researcher himself with little assistance from one trained staff.

KNUST

3.5 DATA ANALYSIS

The data collected was analyzed by using both qualitative and quantitative data methods to assess the extent to which working capital management impact on Hotel Rexmar Limited profitability to conform to conditions established by literary authorities as being necessary for an effective controlling and decision – making process.

The data was analysed through the use of statistical tool such as Pearson Correlation and bar graphs, where appropriate through the help of the Statistical Package for Social Science (SPSS).

3.5.1 Correlation Analysis

This study analyse the effects of accounts receivables period, inventory period, cash conversion efficiency, firm size, firm growth, and leverage on firm profitability.

For the purpose of this study, profitability is measured by Return on Total Assets (ROA), which is defined as profit after interest and tax divided by total assets. This collaborates with the operating income measure of profitability used in the study of Deloof (2003) and is appropriate for this

study. The Hospitality industry is characterised by substantial fixed assets base and relied to a large extent on accounts payable to fund its gross working capital. Thus a comprehensive measure of profitability is best captured by computing the return on total assets which is equal to the total liabilities of the firm (Hotel Rexmar Ltd.), made up mainly of equity capital and current liabilities.

3.5.2 The Explanatory Variables

The efficiency ratios, namely accounts receivable, inventory and accounts payable have been computed, using the formulas as listed in table 6(A). The Cash Conversion Efficiency (CCE) is used as a comprehensive measure of working capital as it shows the time lag between expenditure for the purchases of stock and the collection of sales. The longer the cycle, the larger the funds blocked in working capital. The return on assets is a better measure since it relates the profitability of the business to the asset base. There are many ways of managing return on assets but, in principle, key levers are, of course, profit increase and assets reduction. The latter has become more important to many businesses as the former becomes more elusive.

3.5.3 The Control Variables

In order to account for firm's size and the other variables that may influence profits, accounts receivables period, inventory period, cash conversion efficiency, firm size, firm growth, and leverage and the ratio of current assets to total assets are included as control variables in the Pearson Correlation. The correlation also include the ratio of current liabilities to total assets to measure the degree of aggressive financing policy, with a high ratio being relatively more aggressive.

However, care must be exercised while interpreting the Pearson Correlation coefficients because they cannot provide a reliable indicator of association in a manner which controls for additional explanatory variables. Examining simple bivariate correlation in a conventional matrix does not take account of each variable's correlation with *all* other explanatory variables.

3.5.4 Analysis of Variance (ANOVA)

Single factor Analysis of variance is done on the three components of working capital management: DSO, DIO and DPO to find if the means of the working capital management components are significantly different.

3.5.5 Valuation of the Firm (Value of Operation)

By the application of Thomson's model (2008) of calculating the value of a firm, the value of Hotel Rexmar's value was estimated by:

$$V_{\text{op (at time N)}} = \frac{FCF_1}{(1+WACC)^1} + \frac{FCF_2}{(1+WACC)^2} + \dots + \frac{FCF_{\infty}}{(1+WACC)^{\infty}}$$

Where, FCFs represents free cash flow for periods 2004-2008 and the WACC is the weighted average cost of capital.

The firm's value is the present value of its FCFs, discounted at the weighted average cost of capital (WACC).

The FCFs are the cash flows available to all investors and the WACC is the return required by all investors, so the present value of the FCFs is the value of the firm to all investors.

3.6 ORGANISATION PROFILE

Hotel Rexmar Limited is a private company registered on 27th Day of June 1994.

Their principal place of business is at Odenho Kwadaso, off Santasi Round about and near Opoku Ware School – Kumasi

Their main lines of activities are to provide quality services for Hoteliers, Tourists and Travel Agents, and also the provision of venue for conferences and workshops.

3.6.1 Vision

The vision of Rexmar Hotel Limited is “to be a major quality player in ensuring that continuous, uninterrupted, reliable and safe provisions of hospitality services are provided at the most competitive price.”

3.6.2 Mission

The mission Of Rexmar Hotel Limited is “to use the best practices to build and maintain a healthy player in the hospitality industry”.

3.6.3 Social Responsibility

Rexmar Hotel Limited is socially responsible to ensure that it uses the best practices that are environmentally friendly.

Also it ensures that good quality services and healthy foods are provided for customers.

It occasionally donates books and other accessories to the schools and communities around their business operations.

CHAPTER FOUR

4.0 ANALYSIS AND DISCUSSION OF RESULTS

4.1 PRESENTATION OF DATA AND DISCUSSIONS

Table 1: POSITIONS OF SAMPLED STAFF

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Finance Manager	2	15.4	15.4	15.4
Human Resource Manager	1	7.7	7.7	23.1
Food/Beverages Manager	3	23.1	23.1	46.2
Stores	5	38.5	38.5	84.6
Marketing Manager	2	15.4	15.4	100.0
Total	13	100.0	100.0	

The table 1 above gives a vivid description of the positions of the number of staff sampled for this study. The Finance Department represented 15.4% of respondents, Human Resources Department 7.7%, Foods/Beverages 23.1%, Stores 38.5% and Marketing Department 15.4% respectively. These positions give a picture of how the various departments of Hotel Rexmar Limited are structured and positioned to administer their managerial roles (Appendix 6). From the data given above, it appears that Rexmar is better placed to manage the affairs of the firm.

Table 2: QUALIFICATION OF SAMPLED STAFF

	Frequency	Percent	Valid Percent	Cumulative Percent
Valid Bachelor	4	30.8	30.8	30.8
ACCA,CA,CIM etc	2	15.4	15.4	46.2
HND	5	38.5	38.5	84.6
Others	2	15.4	15.4	100.0
Total	13	100.0	100.0	

The table 2 above shows the description of the qualification of the some top management sampled for the study. This further tells the background of the top management and their ability of managing the working capital of Rexmar. From the data given it appears that the firm is resourced with a good team in their quest in solving the working capital problems.

Table 3: THE COMPANY'S MAIN SUPLIERS

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Akate Farms	1	7.7	9.1	9.1
	Voltic Ghana Ltd	3	23.1	27.3	36.4
	Coca Cola	1	7.7	9.1	45.5
	Gold bird Farms	1	7.7	9.1	54.5
	Santinos Sausages	1	7.7	9.1	63.6
	Blue Banana	2	15.4	18.2	81.8
	Katvico Farms	1	7.7	9.1	90.9
	Darlington Ventures	1	7.7	9.1	100.0
	Total	11	84.6	100.0	
Missing	System	2	15.4		
Total		13	100.0		

The table 3 above gives the description of the main suppliers of Rexmar ranging from the supply of food stuffs to water. This shows that the firm has a number of suppliers, and a good deal with them will go a long to improve the management of the working capital. The questionnaire administered further revealed that on the average the firm receives credit from them ranging between two weeks and one month. An interviewed conducted with the marketing manager indicated that about 15.4% of the purchases comes from the open market. These purchases mainly constitute food stuffs. In conclusion, the credit received from these suppliers/creditors helped the

firm in financing its operations thereby aiding the management of working capital. These data have been displayed in the figure 4.

Table 4: SOURCES OF CASH TO THE COMPANY

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	Bank overdraft	7	53.8	53.8	53.8
	Revenue from sales	6	46.2	46.2	100.0
	Total	13	100.0	100.0	

The table 4 above illustrates the sources of cash in financing the company's working capital. The questionnaire revealed that the company relies greatly on overdraft, which constitutes about 53.8% funds, for financing its operations and for that matter its working capital management. The accountant revealed that the firm has a credit line with their banks which enables the firm get access to these overdrafts anytime a request is made. Another reason why the firm relies on overdraft is that the firm is not able to make enough revenue to cover its operations. In fact, interview conducted with the Accountant revealed that some of the employees' salaries are sometimes in two months arrears.

Table 5: Percentage of the company's budget on operating expenses

		Frequency	Percent	Valid Percent	Cumulative Percent
Valid	20-30	2	15.4	15.4	15.4
	30-40	1	7.7	7.7	23.1
	40-50	9	69.2	69.2	92.3
	Others	1	7.7	7.7	100.0
	Total	13	100.0	100.0	

The table 5 above displays the percentage of the company's budget that goes into operating expenses. The questionnaire revealed that between 40 – 50 % of the company's budget goes into operation. The effort by the company to reduce operating expenses has been mainly by the attempting to reduce waste of materials and bulk purchases to enjoy discounts. Electricity bills alone take about $\frac{1}{3}$ of the operating expenses of the company. The company relies on overdraft to support its operations all year round. This probably explains why the company has reporting poor working capital results.

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The following information also was gathered from the questionnaires administered at Hotel Rexmar Limited:

The company applies the FIFO method in the valuation of its inventories. Reasons given for the choice of this method were for the perishable nature of most of their products and also for consistency with the standards. The company also uses the perpetual inventory taking in its inventory control processes. Management thinks this is the way to check theft and also to check fast moving products and to plan how to investment in them.

It is company policy to give customers between 14 days and 30 days to make payments. However, some of the customers, as revealed by the study, have sometimes failed to pay their bills on time, leading to disputes between them and the company.

The company's main customers are Institutions, tourists and Individuals, with Institutions and tourists forming about 90% of the customers. The mechanism used by the company to trace its credit customers have been the debt aging records and the use of telephone calls. When asked whether these approaches work for company, the accountant replied in the negative.

All authorizations are done by the Managing Director of the company. From the look of things, there seem to be no coordination in the effort of trying to manage working capital. This single handed way of trying to solve working capital problems has not helped the company for the period under review.

4.2 ANALYSIS OF DATA

4.2.1 Days of Inventory Outstanding (DIO)

(Inventory Performance)

From table 6(B), the DIO showed 3.4 days, 2.8 days, 5.0 days, 3.8 days and 2.2 days respectively for periods 2004 – 2008. This rather shows a fluctuating inventory conversion period for Hotel Rexmar Ltd's for the period under review. Using 2004 as the base, the number of days reduced by 18% in 2005, rose by 79% in 2006, reduced again by 24% in 2007 and further reduced by 42% in 2008 (fig. 5). In general Rexmar has on the average 3.5 days to turn its inventory into either cash or receivables.

The trend suggests that Rexmar Hotel has lower inventory turnover and that it has too much inventory on hand. Excess inventory is, of course unproductive and it represents an investment with a low or zero rate of return.

This was revealed in the period between 2007 and 2008. This period showed a reduction of income by 37% (GH¢17,345.99-GH¢10,997.14).

The study reveals that the firm is actually holding damaged or obsolete goods not worth their value.

It is worth noting that, problems arise when calculating and analyzing the inventory turnover ratio. Sales are stated at market prices, so if inventories are carried at cost as they generally are, the calculated turnover overstates the true turnover ratio.

4.2.2 Days of Sales Outstanding (DSO)

(Accounts Receivables Performance)

From the table 6(B) provided for the period (2004-2008) in the question for discussion, there is clear fluctuations in the periods (days) taken by customers to pay their debts when they fall due.

Further analysis revealed that, the number of days given to customers (debtors) rose by 22% and 10% respectively in 2005 and 2006 and reduced by 20% and 39% in 2007 and 2008 respectively (fig. 5).

There was a drop in the number of days given to debtors, which were an improvement in 2007 and 2008, an indication that more cash is recovered. One of course cannot look at these figures in isolation, but should look at the company's credit policy, and that of suppliers.

However, by looking at the credit period granted by suppliers, it proves that Rexmar has, in general, a better deal with suppliers.

4.2.3 Days of Payable Outstanding (DPO)

(Accounts Payables Performance)

The data provided by table 6(B) reveals that the number of days granted to Hotel Rexmar for payment to suppliers rose from 168 days in 2004 to 178 days in 2006. This trend was good for Hotel Rexmar business. As compared with the days of sales outstanding, it gave Rexmar enough room to mobilize funds to settle its debt as and when they fell due.

However, there was a sharp drop in the number of days from 178 days in 2006 to 135 days in 2007 and 97 days in 2008 respectively. One could attribute these drops in the payment periods to the general bad business climate in all sectors in the 2007/08 financial year.

In percentage terms, the trend shows a rise of 1.2% in 2005, 4.7% in 2006, and a drop of 24.2% in 2007 and 28.1% in 2008 (fig. 5).

Notwithstanding, these trends favoured largely the business of Hotel Rexmar. Perhaps, Rexmar would have gone bust due to the global challenges, if it had not received such concession from its suppliers.

4.2.4 Working Capital Ratio

The trend of Hotel Rexmar's working capital ratio (Table 6B) showed a generally negative pattern, meaning that its current liabilities consistently exceeded its current assets throughout the period from 2004 to 2008.

In 2004 there was deficit of 65%, which reduced to 43% in 2005, then rose again in 2006 to 51% and fell to 36% and 34% in 2007 and 2008 respectively.

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This in general terms indicates that Hotel Rexmar has low potential reservoir of funds. Actually, this is proven by the company's cash flow illustrated in table 10.

4.2.5 Cash Conversion Efficiency (CCE)

This ratio was calculated to assess the firm's cash conversion efficiency. Table 6(B) reveals that the cash conversion efficiency has been hovering around 3 – 5 percent. Looking at the figures, it portrays a rather low rate. This implies that it takes a longer time for the firm's inventories or debtors to be converted into cash. This further reveals that cash which is needed for the day to day running of the business is tied up in these resources (inventories and debtors). Refer to figure 5 for the trends in CCE.

4.2.6 Liquidity Position

From table 6(B), the firm's liquidity ratios showed a sharply deteriorating pattern. A close study of the financial statements for the periods from 2004 to 2008 revealed a consistent excess of current liabilities over the firm's current assets.

In the case of current ratio (fig. 6), this reveals that for every one Ghana cedi of current liability Hotel Rexmar had 41 pesewas in 2004; 56 pesewas in 2005; 67 pesewas in 2006; 44 pesewas in 2007 and 37 pesewas in 2008 respectively of current assets to settle its current liabilities. The trend in Acid Test ratio and Cash ratio revealed generally the same pattern. This is simply an indicative of the fact that the firm had less free cash to meet its regular obligation as they fell due.

4.2.7 Interval Measure Ratio (IM)

This particular ratio was calculated to assess Hotel Rexmar's ability to meet its regular cash expenses. For this particular exercise, daily operating expenses covered cost of goods sold plus other operating, administrative expenses and finance charges.

From the figures provided in table 6(B) below, it indicated that Hotel Rexmar had sufficient liquid assets to finance its operations for 43 days in 2004, 60 days in 2005, 146 days in 2006, 39 days in 2007 and 26 days in 2008, even if it does not receive any cash in these periods.

The drastic increase in 2006 (over 100%) is as a result of a loan facility (GH¢9,200) that Rexmar received from its bankers. This cash received led to an increase in the cash and bank balances.

Looking at the trend (fig. 5), it can be stated that it was fairly good for Rexmar since it could pay all its daily operating expenses for at least three (3) months when they fell due.

Table 7 gives the descriptive statistics for the main variables used in this study. Return on assets is on average 5.1 %. Typical to the hospitality industries, the firm has relied mostly on short-term financing; on average the firm collects its receivables after 28 days while they take on average 116 days to pay suppliers. The average CCE is 4%, implying that the conversion rate of resources to cash is very low. The firm's days of inventory outstanding are on the average of 3.4 times a year. This shows a lower turnover, some inventories may go obsolete, holding inventories for more than 106 days. The firm's Growth and Size averaged around 12.3% and 12.4% respectively.

Mean sales value for the firm is GH¢398,420.84. On average about 51% of all assets are financed with financial debt. It is also noteworthy that the average current assets to total assets ratio was

37.6%, thus indicating that greater part of funds are invested in fixed assets leading to a lower operational efficiency.

It is also observed that the variables DPO, DSO and LEV have very large standard deviations that indicate a wide variation in managing these components by the firm.

Empirical Results

Impact of WCM on Profitability

The trends in the figures gotten from table 6B give the vivid impact of working Capital variables on firm profitability. In 2004 for instance, when days of sales outstanding was 26.1 days, the return on total assets was 5.7%. The return on total assets reduced to 4.4% when the days of sales outstanding increased from 26.1 in 2004 to 31.9 in 2005. Again, when the days of sales outstanding further increased to 35 days in 2006, the return on total assets also reduced to 3.6%. In 2007, as the days of sales reduced to 28 days, the return on total assets increased to 7.3%. This result confirms the findings made by shin and Soenen (1998) and Deloof (2003).

This same trends follow hold true for the days of Inventory outstanding for the period 2004 to 2008. Further observation of the days of payables outstanding revealed that, as the days of inventory outstanding increase, return of total assets decreases. This trend is illustrated in the table 6B. Hence, these observations confirm the conclusions made by Deloof (2003).

Furthermore, other variables such as Leverage affect the profitability of the firm. As indicated in the calculations in table 6B, the higher the leverage, the lower the return of total assets and vice versa. The table reveals that, at 52% leverage level, profit was 5.7% in 2004; at 51% leverage level, profit reduced to 4.4% in 2005; at 64% leverage level, profit further reduced to 3.6% in 2006; at 45% leverage level, profit increased to 7.3% in 2007 and at 41% leverage level, profit was

4.5%. These results actually confirming what Myers (2003)'s findings revealed. Refer to figure 8 for the trends in these variables over the period 2004 to 2008.

4.3 ANALYSIS OF VARIANCE (ANOVA)

Single factor Analysis of variance is done on the three components of working capital management: DSO, DIO and DPO to find if the means of the working capital management components are significantly different. Table 8 gives the results of the ANOVA analysis.

The results of this analysis indicate that there is significant evidence that means of the working capital management components (DSO, DIO, and DPO with means 1.152, 1140.22 and 47.0 respectively), widely vary. This means that approaches used by the firm, with respect to managing DSO, DIO and DPO significantly vary.

Since there are significant differences in the means of DSO (fig.1), DIO (fig.2) and DPO (fig.3), the analysis is extended to find which one of these three is significantly different from other. The results of this analysis indicate that there is no significant evidence that a single mean among these key WCM components is significantly different from the two others. All three of these means are significantly different from each other.

This means that no single component significantly contributes to the working capital management efficiency of the firm. For efficient working capital management, the level of DSO should be lower and DPO should be higher. The opposite is observed (DSO, DIO and DPO) in the sampled firm by this analysis. Higher difference between DSO and DPO indicate that there is poor management of both DSO and DPO. This may be due to the intense competition in the hospitality

industry. The firm is unable to set strict collection policies and revenues are made by higher credit sales. Also the hospitality firm is unable to negotiate and get better credit from their suppliers to reduce the DPO. The relationships among these key components of working capital management and the return on assets are shown in the figures 1, 2, and 3 below.

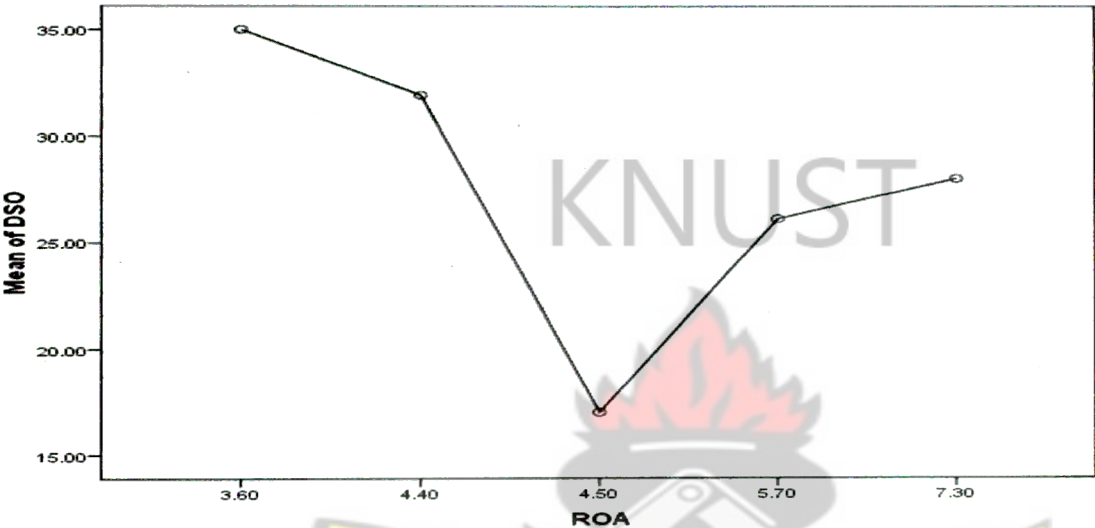


Figure 1: The relationship between DSO and ROA

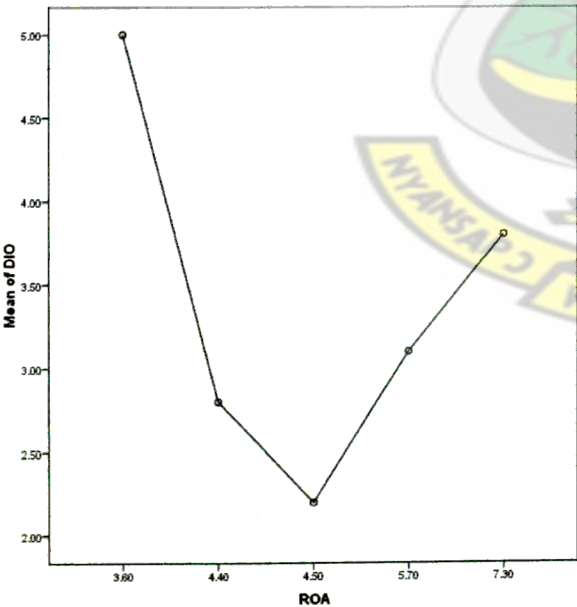


Figure 2: Relationship between DIO and ROA

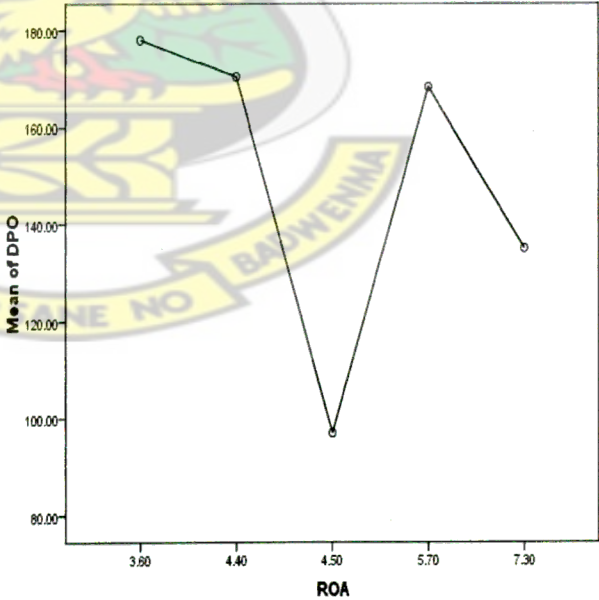


Figure 3: The relationship between DPO and ROA

4.4 CALCULATION OF FREE CASH FLOW

Although Rexmar Hotel Limited's operating capital is projected to produce GH¢9411.56 of after tax profit in 2005, the company needed to invest GH¢17519.45 in new operating capital in 2005 to support its growth plan. Therefore, it was not strange that the free cash flow for 2005 showed a negative of GH¢8107.89.

Research has shown that negative free cash flow in the early years is typical for high growth companies (Thomson 2008). Even though net operating profit after taxes (NOPAT) was positive in all years, free cash is negative because of the need to invest in operating assets (Table10).

The negative free cash flow meant that Rexmar Hotel Limited needed to obtain new funds from stakeholders. Stakeholders will also help fund Rexmar Hotel Ltd., the growth - they need to receive no dividend until after 2010, where the FCF is expected to improve, so all of the net in 2006 needed to be invested. When this free cash flow is invested in current assets, it will improve the working capital base of the firm.

4.4.1 Valuation of the Firm (Value of Operation)

By the application of Thomson's model (2008) of calculating the value of a firm, the value of Hotel Rexmar's has worsened within the period under review (Appendices 1-3). The calculation revealed value of operation (VOP) of (GH¢4006.30). If the NPV shows a positive then it means that WCM has added value to the firm. The negative figure (Table10) indicates the firm's value has worsened, resulting from the low free cash flow from the period 2004 – 2008. This is an indicative of the fact that the working capital had been poorly managed by Rexmar

The result indicates that working capital management has an impact on the firm's value. The empirical findings from the above model indicated that, the management of working capital had a negative effect on the value of Hotel Rexmar. It can therefore be concluded that as working capital is well managed, it affects a firm's profitability and consequently affecting the value of the firm and vice versa.

This confirms the work done by Shin and Soenen (1998) which evidence proved that, firms that manage their working capital more efficiently (i.e., shorter net trade cycle) experience higher operating cash flow and are potentially more valuable.

4.5 CONCLUSIONS OF THE FINDINGS

4.5.1 Determinants of Firm Profitability

In financial management, it is possible to mention that studies regarding working capital management are not as popular as the ones related with capital budgeting and capital structure. From this perspective, this study aims to analyze determinants of firm profitability by means of variables related with working capital management practices using a sample of financial statements of Hotel Rexmar Limited for the period of 2004 – 2008. Empirical results show that, for the mentioned sample and period, days of sales outstanding, days of inventory outstanding and leverage, growth (in sales), size and current assets to total assets significantly and negatively affect profitability of Hotel Rexmar Limited. However, it is also concluded that cash conversion efficiency, has no statistically significant effects on firm profitability of Hotel Rexmar the period of 2004 – 2008.

The results suggest that firm profitability can be increased by shortening days of sales outstanding and days of inventory outstanding. The negative relationship between days of sales outstanding and profitability may be due to that customers need more time to assess quality of products they buy from firms with declining profitability (Deloof, 2003). However, this empirical finding conflicts with some of financial models explaining trade credit. Trade credits are, in general, more profitable short-term investments than marketable securities (Emery, 1984b), so it is rational for, especially, high-profit firms that are more liquid, to transfer relatively high amounts of trade credit to their buyers. Because, according to the liquidity theory, liquid firms are less likely to demand trade credit and more likely to offer it. Another empirical finding is similar, the negative relationship between days of inventory outstanding and profitability and this may be the result of declining sales leading to lower profits and more inventory, as stated in Deloof (2003)'s study.

Leverage is another variable affecting firm profitability negatively. This finding may be explained by the suggestions that highly-leveraged firms are softer competitors that will curtail investment (Myers, 2003), so their insufficient power of competition may lead to decreases in profitability. The only variable in the model of the study that has significantly positive effect on profitability is firm growth (in sales). In of that case the firm may gain some advantages like monopoly or bargaining power due to growth as a reflection of economies of scale (Küster and Demirgünes, 2007); a positive relationship between growth and profitability is expected.

4.5.2 Analysis of Variance (ANOVA) on Key WCM Components

Analysis of working capital management efficiency was done on Hotel Rexmar Limited. The results of this analysis indicate that there is no significant evidence that a single mean among the

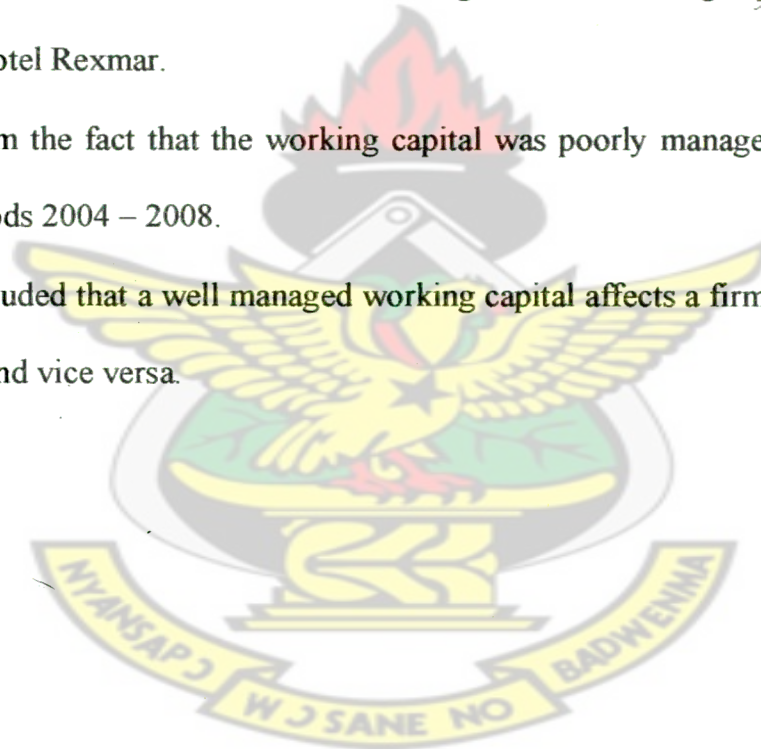
key WCM component is significantly different from the two others. All three of these means are significantly different from each other. When the working capital management efficiency is improved by decreasing days of working capital, there is improvement in profitability of the firm in terms of profit margin.

4.5.3 WCM and Firm's Value

The result indicates that working capital management has an impact on the firm's value. The empirical findings from the model indicate that, the management of working capital had a negative effect on the value of Hotel Rexmar.

This has cumulated from the fact that the working capital was poorly managed leading low free cash flow from the periods 2004 – 2008.

It can therefore be concluded that a well managed working capital affects a firm's profitability and consequently its value and vice versa.



CHAPTER FIVE

5.0 SUMMARY OF FINDINGS, CONCLUSIONS AND RECOMMENDATIONS

5.1 SUMMARY OF FINDINGS

5.1.1 Relationship between Working Capital Management and Firm's Profitability

Empirical findings of the study indicate that days of sales outstanding (DSO) and days of inventory outstanding (DIO), which are directly related variables with working capital management, have significantly negative effects on firm profitability. This means that while days of sales outstanding and days of inventory outstanding lengthen, profitability decreases, or vice versa (Shin and Soenen, 1998 and; Deloof, 2003). The other variables that have significant effects on firm profitability are GROWTH, LEV, SIZE and CA/TA, affecting it positively and negatively, respectively (Table 6B). This means that any increase in sales leads profits to grow, while any increase in debt causes profitability to fall.

5.1.2 Working Capital Management and Firm Value

The result indicates that working capital management has an impact on Hotel Rexmar Limited firm's value. The empirical findings gotten from the Thomson's model (2008) indicates that, the management of working capital for periods 2004 - 2008 had a negative effect on the value of Hotel Rexmar. This means that the poor management of the working capital led to the reduced in the value of the firm. This confirms the work done by Shin and Soenen (1998). It can therefore be concluded that as working capital is well managed, it affects a firm's profitability and consequently affecting the value of the firm and vice versa. In this case the management of working capital Rexmar is not the best, as it's shown in its free cash flow.

5.1.3 Performance of Key Working Capital Management Components

Single factor Analysis of variance is done on the three components of working capital management; DSO, DIO and DPO to find if the means of the working capital management components are significantly different.

Analysis of working capital management efficiency done on Hotel Rexmar Limited indicates that there is no significant evidence that a single mean among the three key components is significantly different from the two others. All three of these means are significantly different from each other. When the working capital management efficiency is improved by decreasing days of working capital, there is improvement in profitability of the firm in terms of profit margin.

5.2 CONCLUSIONS

The different analyses have identified critical management practices and are expected to assist management of Rexmar in identifying areas where they might improve the financial performance of their operation. The results have provided owner-managers with information regarding the basic financial management practices used by their peers and their peers attitudes toward these practices. The working capital needs of an organization change over time as does its internal cash generation rate. As such, the hospitality industries should ensure a good synchronization of its assets and liabilities.

The study revealed that as days of sales outstanding and days of inventory outstanding are lengthened, profitability decreases, or vice versa.

Most of the company's customers delay in making payments and this affect the freed up cash of the organisation. An exclusive interview conducted with the Accountant reviewed that these

have sometimes resulted in disputes with such customers. These issues, he mentioned has been affecting the operations of the organisation, hence the difficulty they have with the working capital management.

It can therefore be concluded that, Rexmar will have to shorten its days of sales outstanding and days of inventory outstanding in order to increase profitability. This can be done by providing incentives such discounts and rebates to induce customers to pay promptly and as well increase the inventory turnover.

5.3 RECOMMENDATIONS

These measures are recommended to help Improve Working Capital Management at Hotel Rexmar Limited:

5.3.1. Proper Cash Flow Forecasting

The essence of effective working capital management is proper cash flow forecasting. Rexmar should take into account the impact of unforeseen events, market cycles, loss of a prime customer, and actions by competitors. The effect of unforeseen demands on working capital should be factored in.

It pays to have contingency plans to tide over unexpected events. While market leaders can manage uncertainty better, Hotel Rexmar Limited must have risk management procedures. These must be based on an objective and realistic view of the role of working capital. This could mean improving credit, billing and cash collections and dealing with disputes effectively, that is

time for legitimate activities like sales, order entry, and cash collection. Overall, efficiency will increase due to reduced operating costs.

Furthermore, Collaborating with the firm's customers instead of being focused only on the firm's own operations will also yield good results. If feasible, helping them to plan their inventory requirements efficiently to match the firm's production with their consumption will help reduce inventory levels. This can be done with suppliers also.

5.3.5. Bridging the Supply Chain

Building greater linkage and closer coordination across the entire supply chain, enabling enhanced demand and supply visibility, elimination of waste, cost reduction and improved service levels.

For example, developing new procurement initiatives, such as working with suppliers to achieve shorter and more reliable lead times, reducing the supplier base to get more leverage in negotiations, developing e-sourcing and building effective relationships with third-party logistics providers will go a long way to improve the working capital of the firm.

5.4 SUGGESTIONS FOR FURTHER STUDIES

This research concludes that there is a pressing need for further empirical studies to be undertaken

on the financial management of the hospitality industries, in particular their working capital practices by extending the sample size so that an industry-wise analysis can help to uncover the factors that explain the better performance for some industries and how these best practices could be extended to the other industries.

This would also assist policy-makers and educators to identify the requirements of, and specific problems faced by hospitality industries in Ghana, especially as more emphasis is placed on the sector by the government. This analysis has been constrained by the sample size and the nature of the data, which could have well affected the results. Further studies will aim at increasing the sample size for still better and consistent panel estimates.

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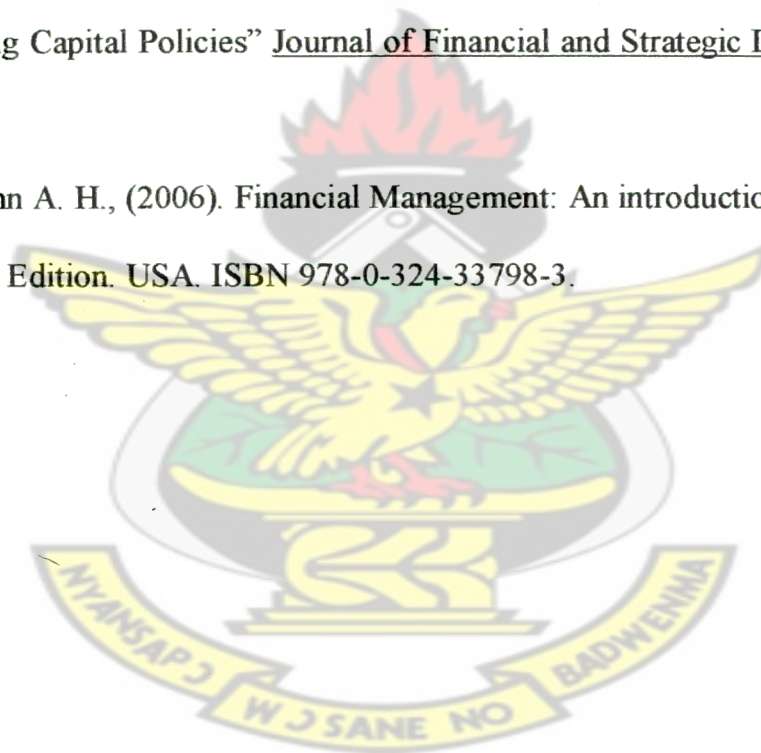


Table 6A. Working Capital Management components definitions

Working Capital Management Component Definitions	
Component	Equation
Days Sales Outstanding (DSO)	Receivables/(Sales/365)
Days Inventory Outstanding (DIO)	Inventories/(Sales/365)
Days Payable Outstanding (DPO)	Payables/(Sales/365)
Days Working Capital (DWC)	DSO + DIO - DPO
Current Ratio (CR)	Current Assets/Current Liabilities
Cash Conversion Efficiency (CCE)	(Cash flow from operations)/Sales
Interval Measure(IM)	CA-INV/Average daily operating expenses
Return on Asset(ROA)	Net Income/Assets
Firm size (SIZE)	$\ln \text{ total assets } [\text{Natural logarithms of total assets}]$
Firm growth (GROWTH)	$\ln \text{ sales} [\text{Natural logarithms of sales}]$
Current Assets/Total Assets(CA/TA)	Current Assets/Total Assets
Leverage (LEV)	Total debt/total assets

Table 6B: Working Capital and other Relevant Ratios

RATIO	2004	2005	2006	2007	2008
CR	0.41	0.56	0.67	0.40	0.37
CCE	0.04	0.03	0.04	0.05	0.03
LEV	52	51	64	45	41
IM	43	60	146	39	26
DIO	3.4	2.8	5.0	3.8	2.2
DSO	26.1	31.9	35	28	17
DPO	168.2	170.3	178	135	97
TD/CA	0.06	0.52	0.25	0.68	0.66
SIZE	12.2	12.3	12.7	12.4	12.4
DWC	*(138.7)	*(135.6)	*(138)	*(103.2)	*(77.8)
ROTA	5.7	4.4	3.6	7.3	4.5
GROWTH	10.43	12.80	12.11	12.95	13.13
CA/TA	0.27	0.41	0.77	0.25	0.18

- Indicates a negative values

Source: Data derived from the Audited financial statements (2004-2008) of Hotel Rexmar Ltd. (Appendices 1, 2 and 3).

Table 7: Descriptive Statistics

	N	Range	Minimum	Maximum	Mean		Std. Deviation	Variance	Skewness	
						Std. Error				Std. Error
	Statistic	Statistic	Statistic	Statistic	Statistic	Error	Statistic	Statistic	Statistic	Error
ROA	5	3.70	3.60	7.30	5.1000	.64420	1.44049	2.075	.966	.913
DIO	5	2.80	2.20	5.00	3.3800	.48000	1.07331	1.152	.831	.913
DSO	5	18.00	17.00	35.00	27.6000	3.06611	6.85602	47.005	-.917	.913
DPO	5	81.00	97.00	178.00	1.4970E2	15.10113	33.76714	1.140E3	-1.210	.913
LEV	5	23.00	41.00	64.00	50.6000	3.90640	8.73499	76.300	.843	.913
GROWTH	5	2.70	10.43	13.13	12.2840	.49463	1.10602	1.223	-1.644	.913
SIZE	5	.50	12.20	12.70	12.4000	.08367	.18708	.035	1.145	.913
CCE	5	.02	.03	.05	.0380	.00374	.00837	.000	.512	.913
CATA	5	.59	.18	.77	.3760	.10534	.23554	.055	1.610	.913
Valid N (listwise)	5									

Table 9: Results of ANOVA for DSO, DIO and DPO

Table 9: ANOVA

	Sum of Squares	df	Mean Square	F	Sig.
DIO Between Groups (Combined)	4.608	4	1.152		
Linear Term Contrast	.038	1	.038		
Deviation	4.570	3	1.523		
Within Groups	.000	0			
Total	4.608	4			
DPO Between Groups (Combined)	4560.880	4	1140.220		
Linear Term Contrast	260.400	1	260.400		
Deviation	4300.480	3	1433.493		
Within Groups	.000	0			
Total	4560.880	4			
DSO Between Groups (Combined)	188.020	4	47.005		

Linear Term Contrast	7.274	1	7.274		
Deviation	180.746	3	60.249		
Within Groups	.000	0			
Total	188.020	4			

Table 10: Calculation of Free Cash Flow

Calculation of Free cash flow	2004	2005	2006	2007	2008
Net operating capital	(6059.91)	(47152.35)	(66317.80)	(59348.55)	(63448.49)
Net Property & Equipment	150189.60	154264.49	181029.35	191406.08	206503.16
Total new operating capital	89592.69	107112.14	114711.55	132057.54	143054.67
Net new investment in operating capital(change in total net operating capital from previous year)		17519.45	7599.41	17345.99	10997.13
NOPAT (Net operating profit after taxes = EBIT(1 – Rate)		9411.56	11580.04	16445.70	11241.16
Less: Investment in operating capital		17519.45	7599.41	17345.99	10997.13
Free Cash Flow		(8107.89)	3980.63	(900.29)	244.03

Source: Data taken from financial statements (2004 - 2008) of Hotel Rexmar Ltd. (Appendix 1, 2, and 3)

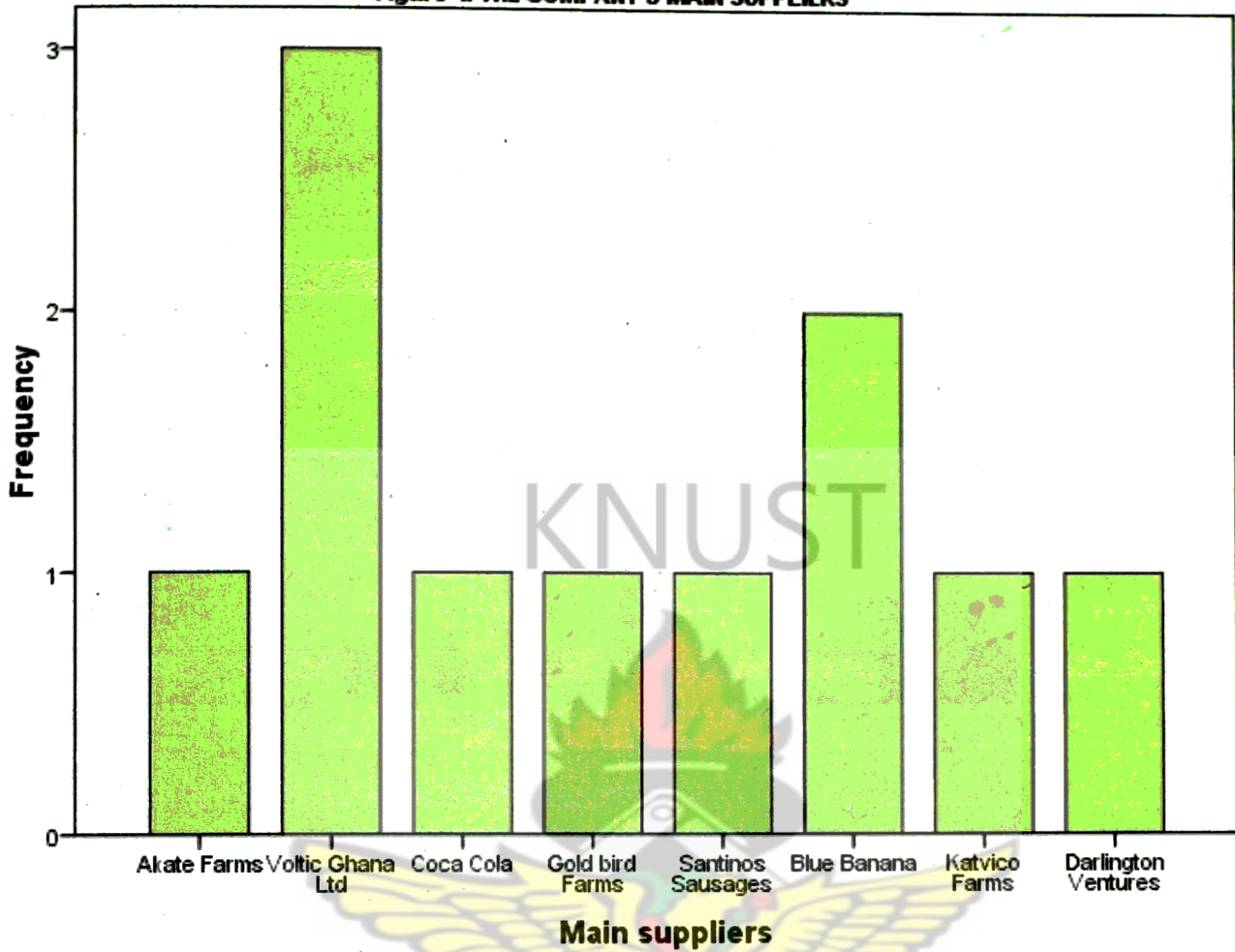
$$\text{Free Cash Flow (FCF)} = \text{GH¢}9411.56 - \text{GH¢}17519.45 = \text{GH¢}8107.89$$

$$\begin{aligned}
 V_{\text{OP (at time N)}} &= \frac{(\text{GHC}8107.89)}{(1+19.4\%)^1} + \frac{\text{GHC}3980.63}{(1+19.4\%)^2} + \frac{(\text{GHC}900.29)}{(1+19.4\%)^3} + \frac{\text{GHC}244.03}{(1+19.4\%)^4} \\
 &= (6790.53) + 3333.86 + (754.01) + 204.38 \\
 &= \underline{\underline{(\text{GH¢}4006.30)}}
 \end{aligned}$$

Weighted Cost of Capital (K_A) = weighted cost of debt + weighted cost of retained earnings

$$K_A = (W_A)(K_D) + (W_E)(K_E)$$

Figure 4: THE COMPANY'S MAIN SUPPLIERS



$$K_A = (25.84)(1-25\%) + 0$$

$$= 19.38\%$$

Weighted cost of retained earnings has been eliminated from this calculation, because the company does not invest its retained earnings.

Figure 5: Working Capital Variables

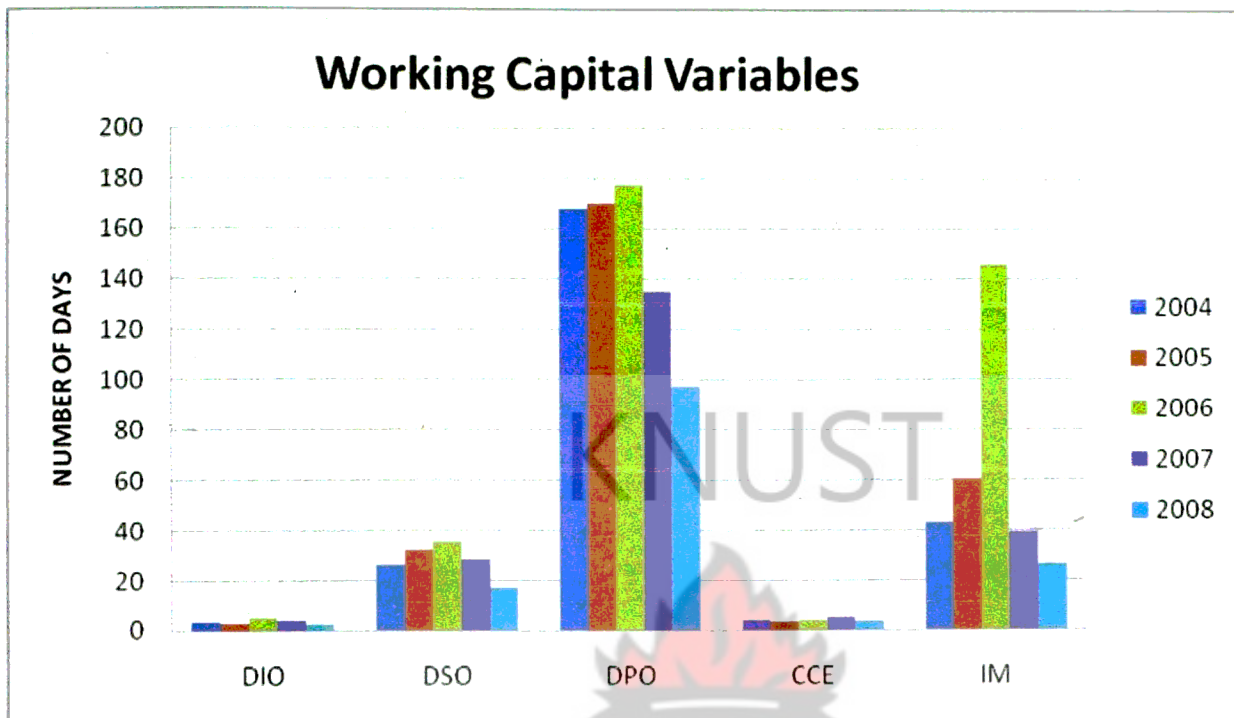


Figure 6: Liquidity Ratios

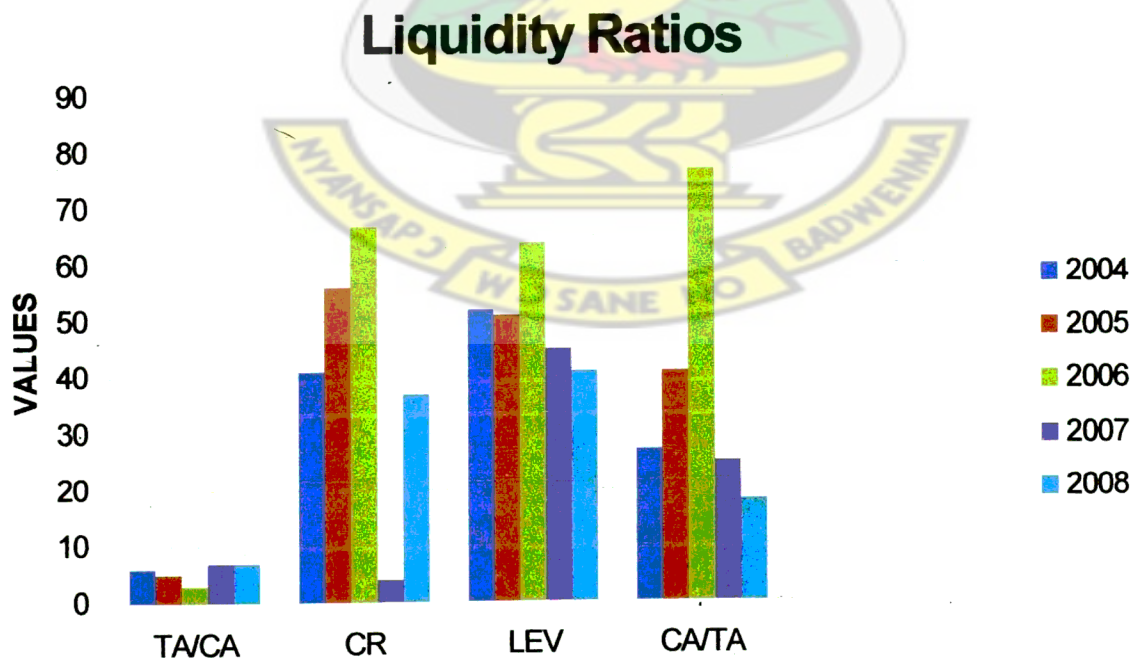


Figure 7: Free Cash Flow from 2005 – 2008

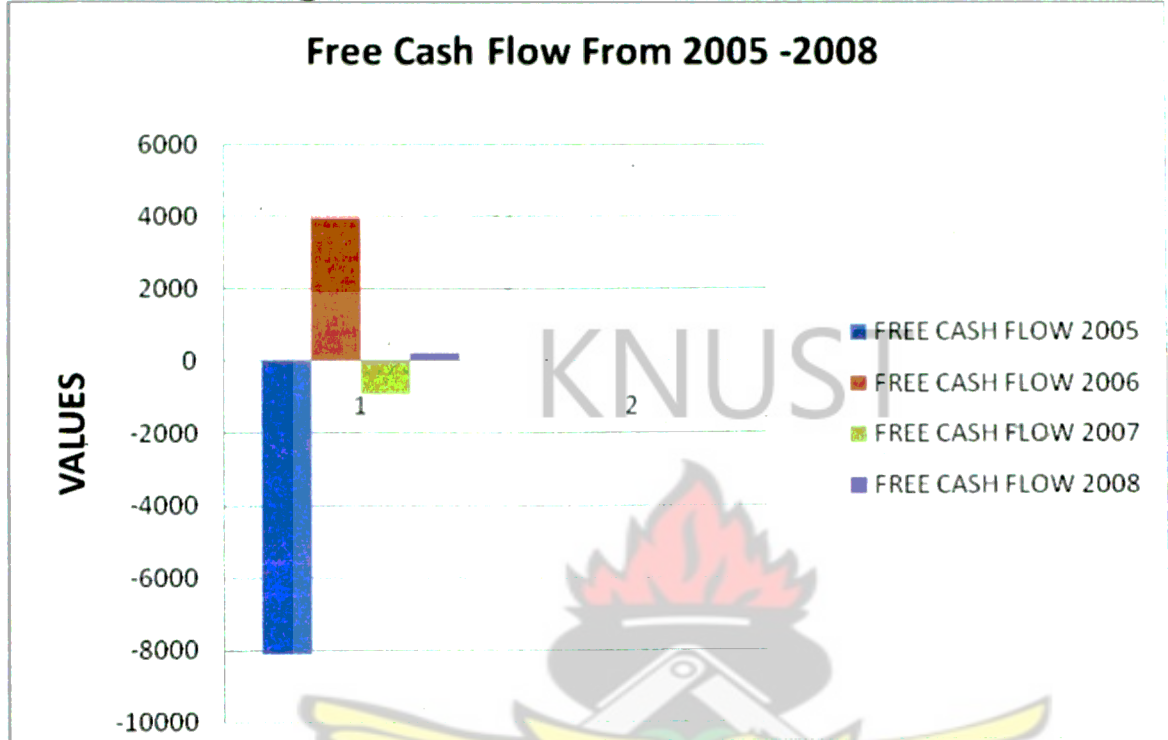
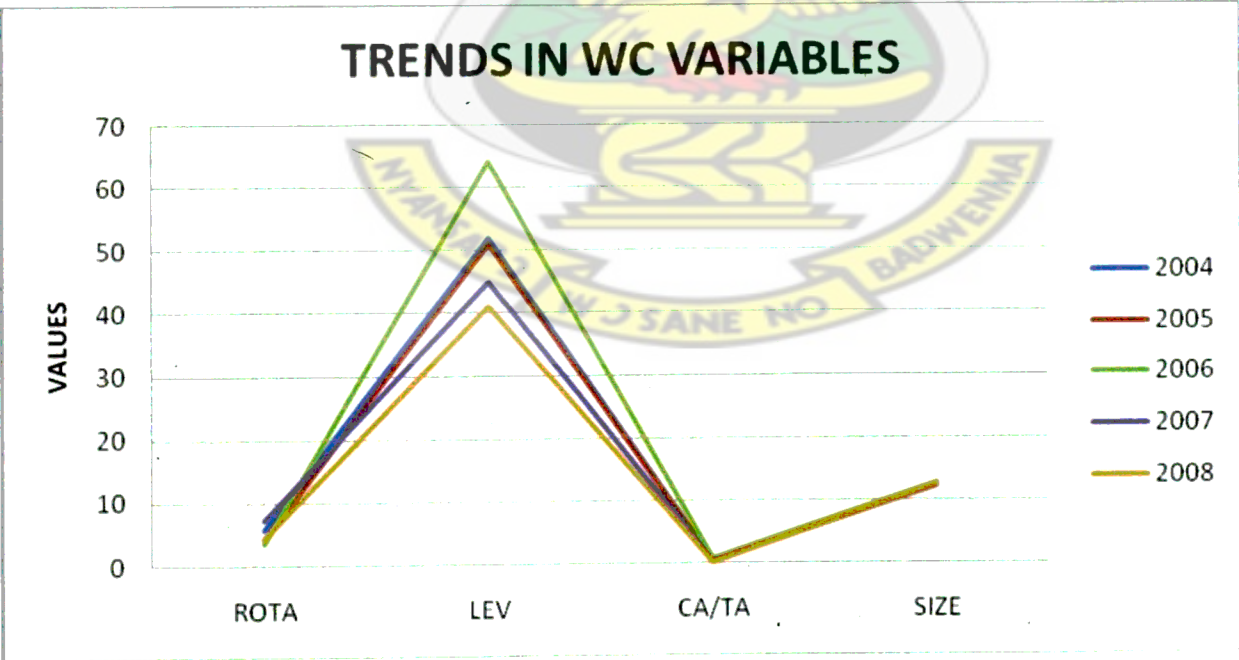


Figure 8: Trends in Working Capital Variables



Appendix 5(a)

QUESTIONNAIRE

WORKING CAPITAL MANAGEMENT AT REXMAR HOTEL LIMITED

NOTE: *The study is for academic purpose only and any information will be held confidential.*

Many questions have been raised as to how firms manage their working capital and whether it has any influence on the Profitability and firm's value.

This study is meant to find out how working capital is managed at REXMAR HOTEL LTD.

You are required to tick responds to the following questions.

SECTION 1: DEMOGRAPHY

1. What is your Functional Position?

.....

2. How long have you been employed in this organization?

(a) 1 – 5 years (b) 6 – 10 years (c) 11 – 15 years (d) 16 – 20 years (e) 20 years or more

3. What is your highest qualification?

(a)	Masters
(b)	Bachelor
(c)	ACCA, CA, CIM etc
(d)	HND
(e)	Others, specify

SECTION 2: COMPANY'S POLICY/ WCM COMPONENTS

4. Who are your customers?

Institutions	1
Tourists	2
Individuals	3
Others	4

5. Do you offer services to any of these on credit?

Yes	1
No	2

6. If yes, how long does it take for them to make payment?

Two weeks	1
One month	2
Three months	3
Others	4

7. What are the key products of your firm?

Restaurant services	1
Terrce Bar services	2
Accommodation/Lodgment	3
Swimming Pool	4
Others, specify	5

8. Which of the products generate the highest returns (Profit)?

Restaurant services	1
Terrce Bar services	2
Accommodation/Lodgment	3
Swimming Pool	4
Others, specify	5

9. Who authorizes purchasing in your company?

Managing Director	1
Accountant	2
Procurement Officer	3
Others, specify	4

10. Are purchases quantities geared to demand forecasts?

Yes	1
No	2
Others, specify	4

11. Do you use order quantities which take account of stock – holding and purchasing costs?

Yes	1
No	2
Others, specify	4

12. Do you have alternative sources of supply?

Yes	1
No	2
Others, specify	4

13. How many of your suppliers have a return policy?

All of them	1
One of them	2
Two of them	3
None of them	4
Others, specify	5

14. Is the company in a position to pass on cost increases quickly through price increases to your customers?

Yes	1
No	2
Others, specify	3

15. If a supplier of goods or services lets you down can you charge back the cost of the delay?

Yes	1
No	2
Others, specify	3

16. How widely available are stocks?

7 – 14 days	1
2 – 7 days	2
Others	3

17. How long does it take for delivery by suppliers?

Two months	1
Three months	2

Others	3
--------	---

18. Can you remove slow movers from your product/services range without compromising best sellers?

Yes	1
No	2
Others	3

SECTION 3: STRUCTURE OF THE COMPANY'S WCM

19. What method is used for the inventory valuation?

FIFO	1
LIFO	2
Weighted Average	3
Standard Price	4
OTHERS, Specify	5

20. Why does the company use the particular method chosen above?

.....

21. Does the company take inventory control?

Yes	1
No	2

22. If yes, which method is used in inventory control?

Periodic inventory taking	1
Perpetual inventory taking	2
Others, specify	3

23. Give reason(s) for the choice of a particular method

.....

24. What mechanism does the company use to trace its credit customers?

Supply – chain management software	1
Debt aging records	2
Others, specify	3

25. How often are major purchases made during the year?

Every week	1
Forth – nightly	2
Every six months	3
Others, specify	4

SECTION 4: COMPANY'S FINANCIAL PERFORMANCE

26. What is the company's average profit generated from operations?

10 – 20	1
20 – 25	2
Above 25	3
Others, specify	4

27. What percentage of company's total assets comprises of current assets?

10 – 20	1
20 – 25	2
Above 25	3
Others, specify	4

28. What percentage of the company's budget goes into operating expenses?

10 – 20	1
20 – 25	2
Above 25	3
Others, specify	4

SECTION 5: CASH MANAGEMENT PRATICES

29. How does the company lodge its cash sales for the day?

By appointed official	1
Collection by Bank official	2

Kept at office safe	3
Others, specify	4

30. When does the company lodge its sales for the day?

At close of day's business	1
Early next day	2
Weekly	3
Others, specify	4

31. Who authorizes cash disbursement?

Managing director	1
Accountant	2
Others, specify	4

32. Which of the following do you use to pay your suppliers/creditors? Please tick those applicable

Cheque	1
Cash	2
Others, specify	4

33. Which of the following is/are applicable to you when making payments to suppliers/creditors? Please tick

Prompt payment	1
Payment in-between credit periods	2
Payment on the last credit period	3
Payment after credit period	4
Others, specify	5

34. Which of the following short-term marketable securities do you hold? Please tick those applicable.

Treasury Bills	1
Certificate of Deposit	2
Commercial paper	3
Others, specify	4

SECTION 6: SOURCE OF FINANCE OF WORKING CAPITAL

35. Which of the following does the company use to finance its working capital?

Credit from suppliers	1
Bank Overdraft	2
Others, specify	4

36. How often does the company rely on overdraft to support its operations?

All year round	1
Quarterly	2
Half – yearly	3
Others, specify	4

37. Who are the company's main suppliers? Please tick those applicable

Akate Farms	1
Voltic Ghana Ltd	2
Coca cola	3
Gold bird Farms	4
Blue Banana	5
Katvico Farms	6
Darlington Ventures	7
Others, specify	8

38. Do you enjoy credit from any of these suppliers?

Yes	1
No	2

39. If yes, how long do they provide the credit?

Two weeks	1
One month	2
Three months	3
Others, specify	4

40. State Any other comments you have

(i).....

(ii).....

(iii).....

(iv).....

(v).....

Appendix 5(b)

INTERVIEW GUIDE

WORKING CAPITAL MANAGEMENT AT REXMAR HOTEL LIMITED

NOTE: *The study is for academic purpose only and any information will be held confidential.*

Many questions have been raised as to how firms manage their working capital and whether it has any influence on the Profitability and firm's value.

This study is meant to find out how working capital is managed at REXMAR HOTEL LTD.

1. What is the procedure for authorizing purchases in the organisation?
2. Looking at your financial report, your current liabilities have consistently been exceeding the current assets, how do you explain this?
3. How does the firm finance its working capital?
4. How often does the company rely on overdraft to support its operations?
5. What means does the firm use in paying its employees?
6. Does the firm sometimes have to pay employees in arrears?
7. Does the firm sometimes have disputes with its suppliers and customers on payments?
8. Which short-term marketable securities do you hold?
9. How is the company able to pass any increases to customers through price increases?
10. If a supplier of goods or services lets you down can you charge back the cost of the delay?

PROFIT AND LOSS ACCOUNT
YEAR ENDED 30TH JUNE, 2005

	(NOTES)	<u>2005</u>	<u>2004</u>
		¢	¢
TURNOVER		<u>3,625,267,955</u>	<u>3,388,832,751</u>
OPERATING COST			
Cost of Goods Sold and Operations	(2)	2,235,996,408	2,164,870,996
General and Admin. Expenses	(3)	1,245,429,869	1,072,937,372
Financial Charges	(4)	<u>18,354,251</u>	<u>16,450,059</u>
		<u>3,499,780,528</u>	<u>3,254,258,327</u>
NET OPERATING PROFIT BEFORE TAXATION		125,487,427	134,574,424
National Reconciliation Levy		(3,137,186)	(3,364,361)
Provision for Taxation	(5)	(28,653,585)	(20,437,070)
NET OPERATING PROFIT AFTER TAXATION		<u>93,696,656</u>	<u>110,772,993</u>
TRANSFERRED TO INCOME SURPLUS ACCOUNT			

INCOME SURPLUS ACCOUNT
YEAR ENDED 30TH JUNE, 2005

	<u>2005</u>	<u>2004</u>
	¢	¢
Balance as at 1st July	836,675,761	725,902,768
Profit for the year	<u>93,696,656</u>	<u>110,772,993</u>
Balance as at 30th June	<u>930,372,417</u>	<u>836,675,761</u>
Per Balance Sheet		

APPENDIX 1(8)
HOTEL KEAMAR LIMITED
BALANCE SHEET
YEAR ENDED 30TH JUNE 2005

	(NOTES)	2005 €	2004 €
FIXED ASSETS	(6)	<u>1,501,895,952</u>	<u>1,542,644,863</u>
CURRENT ASSETS			
Stocks	(7)	27,987,274	31,171,923
Accounts Receivable	(8)	316,703,851	242,702,160
Cash & Bank Balances	(9)	<u>267,148,291</u>	<u>142,281,966</u>
		<u>611,839,416</u>	<u>416,156,049</u>
CURRENT LIABILITIES			
Bank Overdraft		24,612,667	-
Accounts Payable	(10)	1,043,188,299	997,796,501
Taxation	(5)	<u>15,561,985</u>	<u>24,328,650</u>
		<u>1,083,362,951</u>	<u>1,022,125,151</u>
NET CURRENT LIABILITIES		<u>(471,523,535)</u>	<u>(605,969,102)</u>
NET ASSETS		<u>1,030,372,417</u>	<u>936,675,761</u>
REPRESENTED BY:			
STATED CAPITAL	(11)	100,000,000	100,000,000
INCOME SURPLUS		<u>930,372,417</u>	<u>836,675,761</u>
		<u>1,030,372,417</u>	<u>936,675,761</u>

Approved by the Board on:..... 15-12-2005



 DIRECTOR



 DIRECTOR

HOTEL REXMAR LIMITED
CASH FLOW STATEMENT
YEAR ENDED 30TH JUNE, 2005

	<u>2005</u>	<u>2004</u>
	₹	₹
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Profit before Tax & Extra Ordinary Items	125,487,427	134,574,41
Adjustment for :		
Depreciation	102,568,911	99,033,78
National Reconstruction Levy	(3,137,186)	(3,364,36
Interest on Overdraft	180,147	5,106,06
Operating Profit before changes in Working Capital	225,099,299	235,349,93
Changes in Working Capital		
Decrease in Stocks	3,184,649	12,125,55
Increase in Accounts Receivable	(74,001,691)	(137,597,19
Increase in Accounts Payable	45,391,798	46,342,81
Cash Generated from operations	199,674,055	156,221,10
Interest on Overdraft	(180,147)	(5,106,08
Tax Paid	(37,420,250)	(53,494,31
Net Cash Flow from Operating Activities	162,073,658	97,620,70
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of Fixed Assets	(61,820,000)	(21,440,00
Net Cash used in Investing Activities	(61,820,000)	(21,440,00
CASH FLOWS FROM FINANCING ACTIVITIES		
Net Increase in Cash and Cash		
Equivalents	100,253,658	76,180,704
Cash & Cash Equivalents at 1st July	142,281,966	66,101,262
CASH & CASH EQUIVALENTS AT 30 JUNE	242,535,624	142,281,966

HOTEL REXMAR LIMITED
PROFIT AND LOSS ACCOUNT
YEAR ENDED 30TH JUNE, 2006

	(NOTES)	<u>2006</u>	<u>2005</u>
		¢	¢
TURNOVER		<u>3,646,507,684</u>	<u>3,625,267,955</u>
OPERATING COST			
Cost of Goods Sold and Operations	(2)	2,164,018,784	2,235,996,408
General and Admin. Expenses	(3)	1,291,730,903	1,245,429,869
Financial Charges	(4)	<u>36,357,422</u>	<u>18,354,251</u>
		<u>3,492,107,109</u>	<u>3,499,780,528</u>
NET OPERATING PROFIT			
BEFORE TAXATION		154,400,575	125,487,427
National Reconstruction Levy		-	(3,137,186)
Provision for Taxation	(5)	<u>(37,657,500)</u>	<u>(28,653,585)</u>
NET OPERATING PROFIT AFTER TAXATION			
TRANSFERRED TO INCOME SURPLUS ACCOUNT		<u>116,743,075</u>	<u>93,696,656</u>


INCOME SURPLUS ACCOUNT
YEAR ENDED 30TH JUNE, 2006

	<u>2006</u>	<u>2005</u>
	¢	¢
Balance as at 1st July	930,372,417	836,675,761
Profit for the year	<u>116,743,075</u>	<u>93,696,656</u>
Balance as at 30th June		
Per Balance Sheet	<u>1,047,115,492</u>	<u>930,372,417</u>

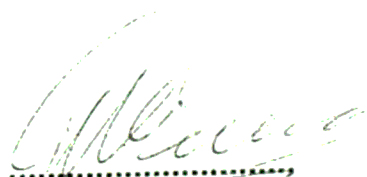
HOTEL CENTAR LIMITED**STATEMENT****AS AT 31 DECEMBER 2006**

	(NOTES)	2006	2005
		€	€
FIXED ASSETS	(5)	<u>1,810,293,480</u>	<u>1,501,895,952</u>
CURRENT ASSETS			
Stocks	(7)	50,096,976	27,987,274
Accounts Receivable	(9)	352,945,789	316,703,851
Cash & Bank Balances	(9)	<u>998,059,863</u>	<u>267,148,291</u>
		<u>1,401,102,628</u>	<u>611,839,416</u>
CURRENT LIABILITIES			
Bank Overdraft	(10)	80,625,645	24,612,667
Accounts Payable	(11)	1,053,687,310	1,043,188,299
Taxation	(5)	9,967,660	15,561,985
Loan	(12)	<u>920,000,000</u>	<u>-</u>
		<u>2,064,280,615</u>	<u>1,083,362,951</u>
NET CURRENT LIABILITIES		<u>(663,177,987)</u>	<u>(471,523,535)</u>
NET ASSETS		<u>1,147,115,493</u>	<u>1,030,372,417</u>
FINANCED BY:			
STATED CAPITAL	(13)	100,000,000	100,000,000
INCOME SURPLUS		<u>1,047,115,492</u>	<u>930,372,417</u>
		<u>1,147,115,492</u>	<u>1,030,372,417</u>

Approved by the Board on: 09 - 11 - 2006



DIRECTOR



DIRECTOR

HOTEL REXMAR LIMITED**CASH FLOW STATEMENT****YEAR ENDED 30TH JUNE, 2006**

	2006	2005
	¢	¢
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Profit Before Tax & Extra Ordinary Items	154,400,575	125,487,427
Adjustment for:		
Depreciation	101,336,914	102,568,911
National Insurance Levy	-	(3,137,186)
Interest on Investment	5,635,718	180,147
Operating Profit before changes in Working Capital	261,373,207	225,099,299
Changes in Working Capital		
(Increase) Decrease in Stocks	(22,109,702)	3,184,649
Increase in Debtors Receivable	(36,241,938)	(74,001,691)
Increase in Creditors Payable	10,499,011	45,391,798
Cash Generated from operations	213,520,578	199,674,055
Interest on Overdraft	(5,635,718)	(180,147)
Tax Paid	(43,251,825)	(37,420,250)
Net Cash Flow from Operating Activities	164,633,035	162,073,658
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of Fixed Assets	(409,734,441)	(61,820,000)
Net Cash used in Investing Activities	(409,734,441)	(61,820,000)
CASH FLOWS FROM FINANCING ACTIVITIES		
Loan Received	920,000,000	-
Net Cash from Financing Activities	920,000,000	-
Net Increase in Cash and Cash Equivalents	674,898,594	100,253,658
Cash & Cash Equivalents at 1st July	242,535,624	142,281,966
CASH & CASH EQUIVALENTS AT 30 JUNE	917,434,218	242,535,624
ANALYSIS OF CASH AND CASH EQUIVALENTS		
Cash Balance	998,059,863	267,148,291
Bank Balance (Overdraft)	(80,625,645)	(24,612,667)
	917,434,218	242,535,624

HOTEL REXMAR LIMITED**PROFIT AND LOSS ACCOUNT****YEAR ENDED 30TH JUNE 2008**

	(NOTES)	2008 GH¢	2007 GH¢
TURNOVER		504,352.26	421,691.05
Cost of Goods Sold and Operations	(2)	<u>(312,562.12)</u>	<u>(254,461.48)</u>
GROSS PROFIT		191,790.14	167,229.57
General and Admin. Expenses	(3)	<u>(173,491.09)</u>	<u>(142,623.04)</u>
Financial Charges	(4)	<u>(3,310.84)</u>	<u>(2,678.93)</u>
NET OPERATING PROFIT BEFORE TAXATION		14,988.21	21,927.60
Provision for Taxation	(5)	<u>(3,991.07)</u>	<u>(4,581.61)</u>
NET OPERATING PROFIT AFTER TAXATION			
TRANSFERRED TO INCOME SURPLUS ACCOUNT		<u>10,997.14</u>	<u>17,345.99</u>

INCOME SURPLUS ACCOUNT**YEAR ENDED 30TH JUNE 2008**

	2008 GH¢	2007 GH¢
Balance as at 1st July	122,057.54	104,711.55
Profit for the year	<u>10,997.14</u>	<u>17,345.99</u>
Balance as at 30th June		
Per Balance Sheet	<u>133,054.68</u>	<u>122,057.54</u>

HOTEL REXMAR LIMITED**BALANCE SHEET****AS AT 30TH JUNE, 2008**

	(NOTES)	2008 GH¢	2007 GH¢
PROPERTY AND EQUIPMENT	(6)	<u>206,503.16</u>	<u>191,406.09</u>
CURRENT ASSETS			
Stocks	(7)	3,018.00	4,436.03
Accounts Receivable	(8)	24,732.52	32,406.50
Cash & Bank Balances	(9)	<u>9,728.29</u>	<u>10,610.90</u>
		<u>37,478.81</u>	<u>47,453.44</u>
CURRENT LIABILITIES			
Bank Overdraft	(10)	14,640.38	11,819.72
Accounts Payable	(11)	83,424.41	94,235.87
Taxation	(5)	<u>2,862.52</u>	<u>746.40</u>
		<u>100,927.30</u>	<u>106,801.99</u>
NET CURRENT LIABILITIES		<u>(63,448.49)</u>	<u>(59,348.55)</u>
NET ASSETS		<u>143,054.68</u>	<u>132,057.54</u>
FINANCED BY:			
STATED CAPITAL	(12)	10,000.00	10,000.00
INCOME SURPLUS		<u>133,054.68</u>	<u>122,057.54</u>
		<u>143,054.68</u>	<u>132,057.54</u>

Approved by the Board on: 29/01/09


 DIRECTOR


 DIRECTOR

HOTEL REXMAR LIMITED**CASH FLOW STATEMENT****YEAR ENDED 30TH JUNE 2008**

	2008 GH¢	2007 GH¢
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Profit before Taxation	14,988.21	21,927.60
Depreciation	12,514.99	11,013.99
Interest on Overdraft	1,988.79	1,876.25
Operating Profit before changes in Working Capital	29,492.00	34,817.85
Changes in Working Capital		
(Increase) / Decrease in Stocks	1,418.03	573.66
(Increase) / Decrease in Accounts Receivable	7,673.98	2,888.08
Increase / (Decrease) in Accounts Payable	(10,811.46)	(11,132.86)
	27,772.55	27,146.72
Interest on Overdraft	(1,988.79)	(1,876.25)
Tax Paid	(1,874.96)	(4,831.97)
Net Cash Flow from Operating Activities	23,908.80	20,438.50
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchase of Property & Equipment	(27,612.07)	(21,390.74)
Net Cash used in Investing Activities	(27,612.07)	(21,390.74)
CASH FLOWS FROM FINANCING ACTIVITIES		
Increase / (Decrease) in Loan	-	(92,000.00)
Net Cash from Financing Activities	-	(92,000.00)
Net Increase(Decrease) in Cash and Cash Equivalents	(3,703.27)	(92,952.24)
Cash & Cash Equivalents at Start	(1,208.82)	91,743.42
Cash & Cash Equivalents at Close	(4,912.09)	(1,208.82)
ANALYSIS OF CASH AND CASH EQUIVALENTS		
Cash Balance	1,979.17	1,312.10
Current Accounts	7,749.12	9,298.80
Bank Overdraft	(14,640.38)	(11,819.72)
	(4,912.09)	(1,208.82)

HOTEL REXMAR LIMITED, KUMASI

ORGANISATIONAL CHART

