An Appraisal of Financial Performance of the Fast Moving Consumer Goods (FMCG) Industry in India

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Abstract

Fast Moving Consumer Goods industry (FMCG) constitutes the fourth largest sector of Indian economy. It is a highly competitive industry which makes a fairly large contribution to the Indian economy in terms of GDP. The financial performance is the blue print of the overall soundness of a business concern, and it also reveals how a business has prospered under the leadership of its management. Numerous studies have been conducted on the evaluation of financial performance of the FMCG firms in India. This study, however takes a fresh look at the financial performance of this sector during the period comprising immediate past five years. Based on the secondary data, the study analyses the FMCG firm's financial performance over the quinquennium starting from 2011-2012 to 2015-2016. The distinct feature of this study is that besides evaluating the financial performance of FMCG firms in India, it also measures the relationship between Sales and Liquidity as well as solvency and profitability of the firms. For testing the hypotheses, the study applies statistical tool of simple regression analysis and computes correlation on SPSS.

Keywords: Financial Performance, Solvency, Profitability, Liquidity.

Introduction

The Fast Moving Consumer Goods Industry is the fourth largest sector of Indian economy. It is highly competitive industry which contributes every year huge part to the Indian economy in terms of GDP. Exploding population of India is the biggest sign for reflecting potential in the market to attract regularly Indian companies as well as foreign MNCs to penetrate the market for earning profit. During the financial year 2015, the revenue generated by FMCG sector was around US$ 9.7 billion. Compounded annual growth of the FMCG market is expected to reach at 13% from financial year 2005 to 2020 the major factors that have contributed to the growth and potential of the FMCG industry include the growth rate of Indian population which has turned India as a large consumer base. The purchasing power of Indian consumers is growing continuously which in turn generates the demand of FMCG products. The other major factor is competition in the market due to which the existing firms are facing difficulty to retain their position, as new FMCG firms are coming regularly which are influencing the established firms to excel in the quality of their products. In 2016 the market size of FMCG is USD 49 billion and it is expected that the share of modern retail will be USD 180 billion in 2020. The Indian FMCG market is full of attractive opportunities due to the direct cash transfer scheme launched by the government of India in rural areas which in turns increases the disposable income of the people over there. Very low portion of the rural market is penetrated by the firms so it's a good opportunity for the firms to enter the market to gain profits. Demand for premium products is increasing in India due to the rising youth population and income level of the people is attracting them towards famous brands. The initiatives taken by the government of India like approving the foreign equity investment level up to 100% in single brand retail and 51% foreign investment level in multi-brand retail and USD 100 millions is the minimum capitalization for foreign companies to invest in India have led to further expansion of FMCG sector. Rural and semi-urban market accounts for 35% of total FMCG market and around 65% of revenue is generated by the urban markets. It is noticed that the rural and semi-urban market is growing rapidly and it is expected that the rural FMCG segment will reach the level of USD 100 billion in 2025.The three major segments of FMCG markets are:

- Personal care and household products (skin care, oral cares, perfumes, paper products, hair care, cosmetics etc).
- Food and beverages products(dairy products, beverages, soft drinks, ice creams, snacks, processed fruits, bakery products, etc).
- Health care (OTC products etc).

Financial Evaluation

It is very important for the firms to manage their financial matters in an efficient way for the success of the enterprises which also helps the firms to retain their position in the market and penetrate into the new market. The financial performance of the firm is very important factor which reflects the financial position of the firm and also the growth of the industry. The financial performance of the FMCG firms is based on the factors such as cost incurred on production of the consumer durable goods and also the revenue and profit generated by the firm. The Financial performance of the firm can be judged with the help of ratio analysis viz liquidity, solvency and profitability etc. With the help of these ratios and financial facts and figures of the firm, we can judge the earning capacity of the firm and how efficiently the firm is using its resources in a particular financial year. For evaluating the financial performance of the FMCG firms, solvency, liquidity, profitability ratios and sales have been taken into consideration in the present study.

Review of Literature

An article authored by Sahu(2002) shows that for the successful functioning of a firm, the role of management is required to focus on maintaining short term liquidity in a scientific manner. The study revealed that the short financial position of the companies in FMCG sector was not satisfactory. An empirical study was conducted by Vishnani and Shah (2007) covering the Indian Consumer Electronics Industry from 1994–95 to 2004–05. From the results of regression analysis it was concluded that working capital management plays an important role in the profitability of an any company. Higher investments in current assets could not yield proper return for the firm which hampered the liquidity and profitability, because huge amount of fund became idle, which thus could not generate any return. Bhunia(2010), In his study on paper producing companies suggested that improper liquidity is major threat for the survival of the firm. Payment of short term obligations reflects the liquidity position of any company.

Another study was conducted by Saleem and Rehman (2011) for the financial year from 2004 to 2009 on selected Oil and Gas companies which were listed on Karachi Stock Exchange. They analyzed profitability by ROA, ROI and ROE and for the liquidity, current ratio quick ratio and liquid ratio were used and it was found that ROA and ROI were significantly influenced by liquidity ratios, However ROI was not significantly affected by Liquidity ratios. Hifza Malik(2011) in the study on determinants of profitability in insurance companies of Pakistan found that there is no relationship between profitability and age of the company, while there is a significant positive association between size of the company and profitability, volume of capital is positively related to profitability while leverage ratio shows negative but significant relationship with profitability. Karamjeet and Firew(2011)studied 449 Indian manufacturing firms and found that there is a significant difference in relative solvency level of firms and their sufficient working capital. Rohit and Vipin (2012) found no relationship between size of firms and liquidity in Indian market of 100 firms during the period 1998-2008.

According to Marimuthu(2012),The ratio analysis technique gives a clear picture about the financial position of any firm. He has suggested in his study that the sample companies reflect up to the mark the current and quick ratios except the interest coverage ratio. His study concluded that the firms should focus on their working capital management properly and maintain receivables, liquidity and payables accordingly. Panigrahi(2013) has suggested that small firms maintain their liquidity more properly than big firms. He has covered a period of ten years in his study. He has focused mainly on the short term financial position of the firms.

Sandhar et.al(2013)investigated the impact of liquidity on profitability of the India cements making firms and found negative relationship between the two. He has analysed the current ratio, liquid ratio, return on asset and return on investment in order to measure the impact of liquidity on profitability. A research on listed companies on Colombo Stock Exchange in Sri Lanka from the food, beverages and tobacco sector was done by Elangkumaran and Karthika (2013) which suggested a significant impact of liquidity on profitability and revealed positive correlation between the two. A study using ANOVA method in automobile companies also suggested that there exists a significant difference between the absolute liquid ratio of the selected sample firms (Sarvanan and Abarna ,2014) Similar relationships were observed between liquidity profitability in the Eljelly's(2004) study of 929 joint stock companies of Saudia Arabia conducted in the year 2004. His study revealed significant negative relationship between the liquidity and profitability ratios. He also found that cash conversion cycle was a better measure of liquidity in comparison to the current ratio.

A recent study was carried by Hetalgaglani and Smita Rao (2015) on financial health of Sun Pharmaceutical Industry Ltd by observing the liquidity and profitability through the application of Altman's Z-score test which depicted a moderate correlation between liquidity and profitability and the sample firms were in green zone.

Research Gap

After an extensive review of literature of empirical works, it is clear that the past researches have probed from the different angles the various aspect of the evaluation of financial performance of FMCG firms. The survey of various studies indicates that no particular study is found having evaluated the financial performance of FMCG firms in India with respect to measuring the impact of sales on the liquidity, solvency and profitability. Therefore, to cover the gap in the earlier studies, the present work is undertaken to give an insight into the financial performance of selected FMCG firms by attempting to offer a detailed examination of the liquidity, solvency and profitability. Moreover, this study also tests the impact of the sales on liquidity, solvency and profitability of the firms.

Objectives of the Study

The objectives of the present study are as follows:

- To evaluate the financial performance of FMCG Industry in India.
- To measure the relationship between Sales and Liquidity position of FMCG firms.
- To investigate the relationship between Sales and Solvency position of FMCG firms.
- To measure the relationship between Sales and Profitability of FMCG firms.

Hypotheses of the Study

In the light of the above objectives, the hypotheses developed for the present study are as follows:

- H01: There is no significant impact of Sales on Liquidity position of selected FMCG firms.
- H02: There is no significant impact of Sales on Solvency position of selected FMCG firms.
- H03: There is no significant impact of Sales on Profitability position of selected FMCG firms.

Research Methodology

A research framework has been developed for this present study which is based on the previous literature. The present study is analytical in nature. The present study is purely based on secondary data and it has been taken from the CMIE prowess data base and financial reports published by the selected FMCG firms which are listed on National Stock Exchange (NSE) in India. For the present study, two major FMCG companies have been selected i.e. Indian Tobacco Company (ITC) limited and Hindustan Unilever (HUL) limited. The period covered by the study is from financial year 2011-2012 to 2015-2016.Financial data of the firms have been analyzed with the help of statistical tools in order to evaluate the financial performance of the selected firms. Measurement of the impact of sales on liquidity, solvency and profitability of the firm has been done with the help of regression analysis.

Data Analysis and Interpretation

Table 1-Descriptive statistics

	Current Ratio	Debt Equity Ratio	Quick Ratio	Return on Assets
Mean	1.46	0.01	0.91	25.36
Median	1.46	0.01	0.87	21.72
Maximum	2.09	0.06	1.36	42.16
Minimum	1.02	0.00	0.62	13.25

Source: Results obtained using E-views software.

The above table-1 depicts the descriptive statistics of selected financial ratios used in the study. As can be seen from the above table, Mean value of ROA for the selected firms is 25.36% with a maximum value of 42.16% and minimum value of 13.25% indicating sound earning capacity of the two firms.

Table 1 show mean value of current ratio and quick ration 1.46 and 0.91 times respectively. It also shows satisfactory liquidity position. However, average current ratio has been lower than the standard of 2:1 and average quick ratio has been lower than the standard of 1:1.

Average solvency ratio of the two firms (0.01) revealed that the selected firms have not made use of debt in their capital structure indicating that they are not trading on equity which might further had increased their profitability.

Table2 -Correlation Matrix

	Quick Ratio	Current Ratio	Debt Equity Ratio	Sales	Return on Asset
Quick Ratio	1				
Current Ratio	.978	1			
Debt Equity Ratio	-0.294	-.378	1		
Sales	.880	.843	-0.143	1	
Return on Asset	.927	.899	-0.290	.968	1

Source: Results obtained using Ms-Excel software.

Table 2- The above correlation matrix reveals a strong positive correlation of sales with liquidity as well as with profitability of the firms under study. However, it can also be noticed that there has been a weak and negative relation of sales with solvency of the firms. Sales had a strong positive correlation of 0.880& 0.843 with quick ratio and current ratio respectively. However there has been a weak negative correlation of 0.143 between sales & debt equity ratio.

Table3 -Regression Analysis on the impact of Sales on Current Ratio

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.202	.293		.688	.511
	SALE	3.208E-006	.000	.843	4.431	.002

Source: Results obtained using SPSS software.
a. Dependent Variable: Current Ratio

Table 3- The above table reflects that sales of the selected firms have been used as regressor and its impact has been analyzed on current ratio which has been used as regressend. Simple regression analysis was conducted to analyze the impact of sales on current ratio. As can be seen, the significance value of the t-statistics of sales is less than 0.05. Hence the null hypothesis i.e. there is no significant impact of sales on liquidity, has been rejected at 5% level of significance.

Table.4 - Regression Analysis of impact of Sales on Quick Ratio

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.149	.152		.982	.355
	SALE	1.958E-006	.000	.880	5.227	.001

Source: Results obtained using SPSS software.
a. Dependent Variable: Quick Ratio

Table.4- The above table shows the result of regression analysis of the sample firms from which it is inferred that the impact of independent variable (sale) on the dependent variable (Quick ratio) is significant. It can be observed that the significant value is 0.001 which is less than the critical value 0.05. Hence the tested null hypothesis has been rejected and it is concluded that there is a significant impact of sale on the quick ratio of the sample firms chosen.

Table.5 - Regression Analysis of impact of Sales on Debt Equity Ratio

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	.021	.023		.911	.389
	SALE	-2.340E-008	.000	-.143	-.408	.694

Source: Results obtained using SPSS software.
a. Dependent Variable: DER

Table-5. The above table represents the analysis conducted with the application of statistical tool of regression analysis to measure the impact of sales on debt-equity ratio of the firm. It is evident that the significance value is 0.694 which is more than the critical value 0.05, hence the null hypothesis has been accepted. It can be seen that the debt equity combination of the firm is not influenced by the sales of the selected FMCG firms.

Table.6- Regression Analysis between Sales and Return on Asset

Model		Unstandardized Coefficients		Standardized Coefficients	t	Sig.
		B	Std. Error	Beta		
1	(Constant)	-11.526	3.478		-3.314	.011
	SALE	9.405E-005	.000	.968	10.954	.000

Source: Results obtained using SPSS software.
a. Dependent Variable: ROA

Table-6. To investigate the impact of sales on profitability of the firm, regression analysis is applied and the above result from the model reveal that the null hypothesis has been rejected because the significance value is 0.000 which is less than the critical value 0.05 and the profitability of the firm is significantly influenced by the sales of the sample of FMCG firms.

Table-7.Summary of Hypotheses Testing

HYPOTHESES	RESULTS
H01: There is no significant impact of Sales on Liquidity position of selected FMCG firms.	Rejected
H02: There is no significant impact of Sales on Solvency position of selected FMCG firms.	Accepted
H03: There is no significant impact of Sales on Profitability position of selected FMCG firms.	Rejected

Finding &Conclusion

The present study deals with the evaluation of financial performance of the selected FMCG firms in India (ITC & HUL).The liquidity position of the firm has been analyzed with the help of the current ratio and quick ratio. The solvency position of the selected firms has been analyzed with the help of debt-equity ratio while for the profitability analysis, return on assets has been used. The study also revealed the impact of sales on liquidity, solvency and profitability of selected FMCG firms with the help of simple regression analyses. The main findings of the study and the conclusion drawn can be summarized as follows.

1. The mean value of profitability of selected FMCG firms during the study period was 25.36 indicating sound return for the shareholder of the company or satisfactory profitability position.
2. Liquidity ratios i.e. quick ratio and current ratio has been a little lower than the standard norms but still firms had a satisfactory liquidity position and have been able to meet short term obligations.
3. Debt-Equity ratio of the selected firms has revealed that the firms have made no use of or a little use of debt in their capital structure. The firms were not trading on equity else they would have further increased their profitability.
4. There has been a strong positive relation of sales with liquidity and profitability of firms with increase in the sales.
5. Sales of the selected FMCG firms have significantly impacted liquidity and profitability of the selected firms. However, sales had no significant impact on their solvency.

Suggestions

Based on findings of the study and conclusion drawn some critical points emerge which are presented in the form of suggestions to improve the financial position of the selected firms.

1. Profitability of the selected firms has been satisfactory during study period. This trend of profitability should be maintained in the future.
2. The current ratio and quick ratio may further be improved by increasing current assets & quick assets or by decreasing current liabilities and the firm should try to maintain the liquidity ratio near the standard level.
3. Selected firms have not used much debt in their capital structure during study period. It is suggested that firms should add more debt in their capital structure or should trade on equity to increase the profit of the companies which in turn shall result in the availability of more profit for the shareholders or owners of the companies.
4. Sales have significantly impacted the liquidity and profitability of the firms during study period. It is suggested that the selected firms should try to increase their sales with the help of various promotional activities by widening their distribution channels and providing proper training to their salesman.

Limitations of the study

The study has some limitations which can be addressed in further studies. The present study is mainly based on secondary data and all the aspects of financial performance have not been taken into account. The current study covers the period of five years only and it is confined to selected FMCG firms in India only.

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